97th Congress
2d Session

COMMITTEE PRINT

SECOND MEETING

OF THE

COMMITTEE ON SMALL BUSINESS

UNITED STATES SENATE

WITH

MEMBERS

OF THE

COMMITTEE'S NATIONAL ADVISORY COUNCIL

APRIL 22, 1982

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COMMITTEE ON SMALL BUSINESS

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In July 1981, the Senate Committee on Small Business established a National Advisory Council in order to bring the "grassroots" small business viewpoint to Congress. The Council is made up of 25 small business owners/operators from around the country; individual council members, representing a broad range of business interests, pay all of their own expenses to attend meetings with the Committee.

On Thursday, April 22, 1982, the National Advisory Council held its second meeting with Members of the Committee on Small Business. We believe that the meeting was extremely worthwhile. It provided the Members of this Committee with the small business community's views on a number of important issues, including: export promotion; economic development; small business innovation and research activities; antitrust policy; debt equity regulations; and the U.S. economic climate in general. During its meeting, the National Advisory Council passed a resolution calling for the repeal of Section 385 of the Internal Revenue Code (relating to the definition of debt and equity for Federal Income Tax purposes) and for the Senate Finance Committee to hold hearings on this critical small business issue.

On behalf of the entire Committee, we would like to extend our gratitude to the National Advisory Council members for their counsel and advice. We value the opinions and suggestions of the Council and look forward to our next joint meeting.

Sincerely,

LOWELL WEICKER, JR.,
Chairman.

SAM NUNN,
Ranking Minority Member.

SECOND MEETING

THURSDAY, APRIL 22, 1982

U.S. SENATE,
COMMITTEE ON SMALL BUSINESS,
Washington, D.C.

The committee met, pursuant to notice, at 2:10 p.m., in room 424, Russell Senate Office Building, Hon. Lowell Weicker, Jr. (chairman of the committee), presiding.

Present: Senators Weicker, Hayakawa, Nunn, Huddleston, Levin, and Dixon.

Also present: Robert J. Dotchin, staff director; R. Michael Haynes, chief counsel; Kimberly A. Elliott, professional staff member; Brian F. Hartman, financial analyst; Robert M. Wilson, counsel; and Alan L. Chvotkin, minority chief counsel.

Mr. MUDGE. Thank you for coming on time and for preparing some material for the committee to consider. I would like to call on Glenn Stout to discuss the first item on the agenda.

REPORT ON EXPORT PROMOTION

Mr. STOUT. Mr. Chairman and fellow members of the National Advisory Council: To start with, item 3 on the fact sheet has a negative air about it which reflects the general attitude toward small business-exporting policies and information that we see published. In my allotted time on the subject, I want to discuss some deep concerns I have about the ability of small U.S. businesses to become involved in international trade. Let me give you the bottom line first and then I will expound on some key components which I feel bring us to these bottom line conclusions.

First of all: Item A, Information from the Federal Government. The U.S. Government needs to improve the procedures and communication lines for channeling information to small businesses on how they can become involved in exporting.

It is true that the Government sponsors occasional meetings, provides many publications, regional counseling centers, and other spurious information; all are targeted primarily for big business and are not prepared to assist the small businessman, in his terms and at his level. It would seem prudent business for the Government to strive to better coordinate, accelerate, and expand its efforts to communicate directly to the small business segment on exporting procedures and activities.

Item B: U.S. Government cooperation in the export process for small business. The small business share of the gross national product is steadily declining. At the same time, the number of small busi-

nesses have been increasing. Small business employment is increasing, and the percentage of new hires has been increasing, except for the recent surge in bankruptcies and closings attributable to the present economy. Export promotion can be a vehicle for small business to increase their sales share.

Foreign governments take a very active role in promoting and aiding in exports for their businesses in many ways as we have all observed. These include subsidies, equivalent market access, and being a partner to business in export promotion. Our Government must take a more aggressive role in removing existing barriers to exporting, in developing overseas markets and, in general, preparing and educating the American people from the elementary school level upward so that they understand and are prepared for world commerce, and develop an export mentality. Without increased activity in these areas, our ability to successfully compete will continue to erode.

Item C: Government development of stable, long-term long-range programs. As a small business person, I cannot seriously think about establishing long-term commitments for export promotion with on-again off-again export rules, regulations, and incentives. We simply must move away from a year-to-year, sometimes month-to-month, style of Government action or inaction. In other words, we must depoliticize the process of international trade, and, like virtually all other international competitors, we must knuckle down together to the business of selling American products everywhere and anywhere they can be sold, competing successfully head-to-head with any other nation in the world. Not all small businesses are in a position to, or desire to, export. However, those who have export potential are hesitant because of real and imagined barriers.

Export trade, unlike domestic trade, is not free and easy trade. It requires dealing with myriads of regulations, substantial paperwork, bureaucratic entanglements, and too often, requires the assistance of international legal assistance.

So to state again, for small business to increase to exporting capabilities; we need three basic areas of Government support and intervention, as follows: (a) information from the Government; (b) Government cooperation in the export process; (c) Government development of stable, long-range, depoliticized programs and policies for export.

There are many components of these three categories. However, due to the time constraint imposed by Mr. Mudge, I will mention, only briefly, a few of these components at this time. I have prepared a handout with an expansion of each component, which I believe each of you now has.

First of all, with respect to information from the Government, the Small Business Administration does not take initative actions on exports. The agency is content to only react and supply information when asked. The Department of Commerce possesses a tremendous wealth of information, well writen and easily understood, such as "A Basic Guide to exporting" booklet that is available. The problem is the lack of focus on the small business segment. The Government should make available information for foreign joint venture programs with foreign companies or foreign governments, and provide a guide

to the requirements of each of the governments for the foreign partner to meet. Presently, this can only be obtained from a lawyer or the government in each specific country.

With respect to Government cooperation in the export process, first we should reduce constraints on the Export-Import Bank. Second, we should support legislation which will improve barter and export trading companies, such as S. 734, H.R. 1799, and H.R. 1648. Third, Government support may be required to initiate a program in the lower school grades for a second compulsory language requirement, as well as for other subjects which would help develop foreign business. Fourth, our Government should consider adopting programs similar to those of foreign governments, wherein the Government becomes an active participant or partner in a venture targeted for export promotion.

With respect to the development of stable, long-term long-range Federal export programs: First, we should consider short-term low-interest loan programs specifically targeted for small business export sales; second, we should consider tax relief on inventory, direct labor costs, and work-in-process which is foreign destined—I would also say that in this area, I have related that to an on-site trade zone, within the company itself; third, we should stabilize and update Government intentions, policies, rules and regulations toward international business; fourth, we should urge the administration to remain behind the General Agreement on Tariffs and Trade; fifth, we should strengthen the Foreign Corrupt Practices Act with clear and concise language—the Chaffee amendment, S. 708, passed the Senate but is now hung up in the House on political issues, and it should be cleared as soon as possible; and sixth, we should preserve the Domestic International Sales Corp.

Why should we be concerned with increasing exports? There are some very obvious reasons I would like to touch upon here which are not in my prepared statement. First, the U.S. population growth is continuing to decrease, which will result in smaller domestic markets. If we want to maintain our standard of living, we must makes sales elsewhere.

Second, the educational explosion in America is shrinking our traditional unskilled manual labor force, so that by the year 2000 it will be practically nonexistent. We will be forced to export machine-made piece parts, textiles, chemicals, raw materials, and so forth, to integrate the low-cost labor resources of the Third World into subassemblies and components, which will then be returned for our final finishing, assembling, testing, and packaging for domestic as well as foreign markets.

Third, production sharing with the Third World developing nations will create purchasing power within those nations, creating an export market for our finished goods which can, of necessity, only be furnished by a higher-technology producing nation.

Fourth, I leave for last, the explanation that we must begin to learn international trade procedures now so that we will be able to take advantage of the developing situations I have just described, in our world of competitive coexistence. In the past, we have been familiar with the national economy. The trend is toward a polycentric economy, which is a world economy with no one clear leader, but a number of major economic centers living together in competitive coexistence.

In closing, I would like to refer to the fact that the President's report to Congress on "The State of Small Business" was a book of some 360 pages, yet only 1½ pages were devoted to international trade. On page 172 of this document, there were several references to complex laws, substantial paperwork, bureaucratic procedures, and difficult barriers, all of which seemed to be saying: "Small business, international trade is not for you." The only bright glimmer was the reference to the 1980 enactment of the Small Business Export Expansion Act. This act "directs the SBA and the Department of Commerce to provide educational and marketing assistance and to improve access to export information and assistance for small business." However, when questioned about this, the Minneapolis regional SBA office representative told me, "The SBA has no funds for export programs."

Mr. Chairman, members of the committee, I realize my statements have been much too brief for the comprehensive and innovative effort to introduce small businesses into export trade. Thank you for the opportunity to speak on this subject. If anybody has any questions, I will do my best to answer them.

Mr. MUDGE. We have 10 minutes on this subject, if anyone would like to comment on it. The other material Mr. Stout has is for reference purposes.

Senator WEICKER. I do not want our lack of questions to indicate any lack of interest. What some of us are trying to do here is to listen.

I happen to agree with you 100 percent that this is the most important area for small business, and the most difficult. As Shaw will tell you, his family was in international business, and indeed so was mine, long before international business among large corporations became popular or presented profit opportunities. Indeed, that is the reason why I was not born in the United States. Those are some of the reasons that I am so attuned to exporting.

It is only within the last few decades that big business has become actively involved in international trade. Clearly, small business lags behind, for obvious reasons, including obtaining the capital required, and getting advice on how to export. Yet there is no question in my mind that for most of our large businesses, the bottom-line profits are being generated in international trade; there is no question about that. You just have to take a look at the annual reports to see how much of their profits are coming from abroad.

Mr. STOUT. One of the problems that we have is, there is a lot of opposition to trade agreements for the business of the United States. I think primarily, since I do export quite a bit and have made many trips to other countries, that when governments and businesses in foreign countries look at the United States, they see a united front of big business facing them. If in some of our legislation and trade agreements we could make an offset between their small businesses and our small businesses, for an equalization of trade between small businesses, so that their small businesses do not have to appear to be supported by their governments, they can compete with our small businesses in world trade. We may solicit their cooperation and interest a little more if we are concerned with their small businesses as well.

This has never been done. Everything that is written, all the approaches that are taken to international trade focus solely on big business. You will never find the words "small business" included any place

in a portion of an agreement or a trade arrangement. At least I have never seen one.

Senator WEICKER. I do not mean to bog down the discussion or to monopolize it. If anybody else wants to jump in, they can.

There was an article which stated that the General Electric Corp. is setting up an entirely new subsidiary, making available their international contacts and their international expertise to small businesses around the United States. Did anybody else see the article I am talking about? I wonder if you feel that private sector efforts, such as the G.E. effort, are going to be adequate, or does there have to be direct Government involvement?

Mr. STOUT. G.E. is still a large business, and it looks like they are fronting with a small one. Of course, G.E. charges for this.

Senator WEICKER. That is what I am saying. They are doing it as a business.

Mr. STOUT. In days gone by, in foreign countries, if something was made by Singer of Kodak, or if it was Cellophane or something like that, it smacked of a good product or a well-known product. Foreign countries like this. However, that image is beginning to go away now, and foreign countries are looking for technology updates and product developments that are coming out of the small business sector.

One of the things that we must remember is that National Semiconductor and Intel and Control Data were all small businesses at one time. They were leaders in exporting U.S. technology to foreign countries; foreign countries that started out building one small part and selling it back to us at a very favorable rate. Then they took the next step, by putting that one small component into a larger assembly.

Let us take the computer, for instance. Foreign nations started out building the switches and the printwheels. Then they started manufacturing print heads. Next they built keyboards and parts of floppy disc mechanisms. Now what has happened is, because we have bought so much of that material from foreign countries, we have given them the flywheel effect in production and development and sales, and it has established them in the business much less expensively than what we could have done ourselves. Now they are coming to our marketplace with computers that directly compete with our Apples and IBM's, Xeroxes, and so forth. But it has been our production needs and our purchases that have put them in U.S. markets.

That leads into quite a different subject of trading, protecting our patents and our technology. But I think that if we could work with foreign nations on a small business to small business basis, and keep the General Electrics out of it, it would work. However, there would have to be strong dedication on the part of our Government that this is our intent.

Mr. MUDGE. There have been three bills, Glenn, and I wonder if you want to comment on any one of them. We have four minutes left on the subject, unfortunately. There is the Export Trading Company Act, which pased the Senate 93 to 0 last year; S. 795 or H.R. 5235, to exclude exports from antitrust regulations, on which the Judiciary committee held hearings in June of last year; and S. 868 or H.R. 3228, Competitive Export Financing Act, which was reported out by the Banking, Housing and Urban Affairs Committee in July. Have you given any thought to those bills, and do you have any comments for us here?

93-677 O - 82 - 2

Mr. STOUT. Yes. Export trading companies and joint ventures are going to be vital if we are, as I said earlier, going to interface with the Southeast Asia and east Asia areas, where the workshops of the future are going to be. There is a paper included in my report, published by MACI, the Minnesota Association of Commerce and Industry, which does go into this issue in more detail. Rather than my reiterating that report, I have attached their very excellent paper for reference.

[Material follows:]

UNITED STATES SENATE

COMMITTEE ON SMALL BUSINESS

April 22, 1982 Meeting of the

NATIONAL ADVISORY COUNCIL TO

THE SENATE COMMITTEE ON SMALL BUSINESS

E X P O R T P R O M O T I O N

By

Glenn M. Stout

EXPORT PROMOTION

Mr. Chairman, Members of the Committee and Fellow Members of the National Advisory Council.

In my allotted few precious minutes on the subject of EXPORT PROMOTION, I want to discuss some deep concerns I have about the ability of small business throughout America to become involved in International Trade.

Let me give you the bottom line first, and then some key components which I feel bring us to those bottom line conclusions.

A. INFORMATION FROM GOVERNMENT

The U.S. Government and its departments need to improve the procedures and communication lines to channel information to the small businesses on how they can become involved in exporting.

It is true there are occasional meetings, many publications, regional counseling centers and other spurious information, all primarily targeted for big business and not prepared in the context of "Talking to the small businessman in his terms and at his level." It would seem prudent business for the Government to strive to better coordinate, accelerate and expand its efforts to communicate directly to the small business segment on exporting procedures and activity.

B. U.S. GOVERNMENT COOPERATION IN THE EXPORT PROCESS FOR SMALL BUSINESS.

The small business share of the G.N.P. is steadily declining. At the same time, the number of small businesses have been increasing. Small business employment is increasing, and the percentage of new hires has been increasing (except for the recent up-surge in bankruptcies and closings attributable to the present economy). Export promotion can be a vehicle for small business to increase their sales share.

Foreign governments take a very active role in promoting and aiding in exports for their businesses in many ways we have all observed such as subsidies, equivalent market access and being a partner to business in export promotion. Our Government must take a more aggressive role in removing existing barriers, in developing overseas markets, and in general prepare and educate the American people from the elementary school level upward to understand and be prepared for world commerce, and to develop an export mentality. Without increased activity in these areas, our ability to successfully compete will continue to erode.

C. GOVERNMENT DEVELOPMENT OF STABLE, LONG TERM, LONG RANGE PROGRAMS

As a small business person, and millions of others like me, I can't think seriously about establishing long term commitments for export promotion with on-again, off-again export rules, regulations and incentives.

We simply must move away from a year to year, sometimes month to month, style of government action or inaction. In other words, we must de-politicize the process of International trade, and, like virtually all other International competitors, we must nuckle down together to the business of selling American products everywhere and anywhere they can be sold, competing successfully head-to-head with any other nation in the world. Not all small businesses are in a position to, or desire to, export. However, those who have export potential are hesitant because of real and imagined barriers.

Export trade, unlike domestic trade, is not free and easy trade. It requires dealing with myriads of regulations, substantial paperwork, bureaucratic entanglements and too often requires the assistance of International legal assistance.

So to state again, for Small Business to increase exports, we need three basic areas of government support and intervention as follows:

A. Information from Government.

B. Government cooperation in the export process.

C. Government development of stable, long range de-politicized programs and policies for export.

There are many components of these three categories. Because of the time constraint imposed by Mr. Mudge, I will mention, only briefly, a few of these components at this time. I have prepared a handout with an expansion of each component, which I believe each of you now has.

A. INFORMATION FROM GOVERNMENT:

1. The Small Business Administration does not take initiative action on exports. They are content to only react and supply information when asked.
2. Department of Commerce
   They possess a tremendous wealth of information, well written and easily understood such as "A basic Guide to Exporting". The problem is the lack of focus on the small business segment.
3. Make available information for foreign joint venture programs with foreign companies or foreign governments through a guide to the requirements of each of the governments for the foreign partner to meet. Presently this can only be obtained from a lawyer or the government in each specific country.

B. GOVERNMENT COOPERATION IN THE EXPORT PROCESS

1. Reduce contraints on the export-import bank.
2. Support legislation which will improve barter and export trading companies such as S734 HR1799 and HR1648.
3. Government support may be required to initiate a program in the lower school grades for a second compulsory language requirement. Also, other Subjects which would help to develop foreign business.

4. Our Government should consider adopting programs similar to those of foreign governments wherein the government becomes an active participant or partner in a venture targeted for export promotion.

C. GOVERNMENT DEVELOPMENT OF STABLE, LONG TERM, LONG RANGE PROGRAMS.

1. Consideration of short term, low interest loan programs specifically for small business export sales.
2. Consideration for tax relief on inventory, direct labor costs and work-in-process which is foreign destined.
3. Stabilize and up-date government intentions, policies, rules and regulations toward International business.
4. Urge the administration to remain behind GATT (General Agreement on Tariffs and Trade)
5. Stabilize The Foreign Corrupt Practices Act with clear and concise language. The Chaffee Amendment, S-708, passed the Senate, but is now hung up in the House on political issues. This should be cleared as soon as possible.
6. Preserve the DISC (Domestic International Sales Corp.)

In closing, I would like to refer to the fact that the President's report to Congress on "The State of Small Business" was a book of some 360 pages, yet only 1-1/2 pages were devoted to International Trade. On page 172 of this document, there were several references to complex laws, substantial paperwork, bureaucratic procedures and difficult barriers, all which seemed to indicate, "Small Business, International Trade is not for you". The only bright glimmer was the reference to the 1980 enactment of the Small Business Export Expansion Act. This Act "Directs the SBA and the Department of Commerce to provide educational and marketing assistance and to improve access to export information and assistance for small business." However, when

questioned about this, the Minneapolis Regional SBA office representative told me, "The SBA has no funds for export programs."

Mr. Chairman, Members of the Committee, I realize my statements have been much too brief for the comprehensive and innovative effort to initialize small business into export trade.

Thank you for the opportunity to speak on this subject.

UNITED STATES SENATE

COMMITTEE ON SMALL BUSINESS

April 22, 1982 Meeting of the

NATIONAL ADVISORY COUNCIL TO

THE SENATE COMMITTEE ON SMALL BUSINESS

SUPPLEMENTAL INFORMATION TO

THE ORAL PRESENTATION

ON

E X P O R T P R O M O T I O N

By

Glenn M. Stout

93-677 O - 82 - 3

SMALL BUSINESS

EXPORT PROMOTION

The idea of a small business entering into export trade can be frightening; especially for an owner or manager who has never made foreign business contacts, does not speak any foreign languages, has trouble properly executing domestic government paperwork and forms and is enjoying a prospering business without exporting.

A big share of the small local service and supply type businesses definitely do not belong in the export business. There are, however, many manufacturing and technically based small companies who could and should export.

Why should we be concerned with increasing exports? For very obvious reasons:

1. The U.S. population growth is continuing to decrease, which will result in smaller home markets. If we want to maintain our standard of living, we must make sales elsewhere.

2. The educational explosion in America is shrinking our traditional unskilled manual labor force, so that by the year 2000 it will be practically nonexistent. We will be forced to export machine-made piece parts, textiles, chemicals, raw materials, etc. to integrate the low cost labor resources of the third world into sub-assemblies and components which will be returned for our final finishing, assembly, testing and packaging for our domestic as well as foreign markets.

3. Production sharing with third world developing nations will create purchasing power within those nations, creating an export market for our finished goods which can, of necessity, only be finished in a higher technology producing nation.

4. I leave for last the explanation that we must begin to learn the International Trade procedures now to be able to take advantage ofthe above developing situations, and exist in a world of "Competitive coexistence".

   In the past we have been familiar with "National economy". The trend is toward a "Polycentric economy", which is a world economy with no one clear leader, but a number of major centers living together in competitive coexistence.

A small business wishing to explore export possibilities may find comfort in the fact that a large share of our exports stay in North America (Canada and Mexico).

For the prospective exporter there are four initial basic rules to remember:

1. Maintain a neutral stance in the area of foreign government relations.

2. Establish a bargaining position.

3. Enlist and use local participation wherever and whenever possible.

4. Balance local dependency with worldwide scope.

Regardless of the desire to export, the opportunities which exist and the need to expand markets, I have some concerns for small business to become involved in International Trade.

Traditionally, foreign governments have provided strong support for their exporting companies. For example, foreign government representatives are expected to provide marketing leads, political leverage and persuasive follow-up aid for their nations' exporters. U.S. Government representatives do not provide this level of support for American firms. This leads to my concerns as follows:

A. INFORMATION FROM GOVERNMENT

1. The Small Business Administration

Small business should receive information and counselling from the S.B.A. on all related small business subjects. Unfortunately there is no initiative action program within the S.B.A. to provide information on export promotion programs. In fact, the S.B.A. has stated they have no funds for export promotion.

A recent news release by the U.S. Chamber of Commerce stated that this year the U.S. Government will spend more than $100 million on trade promotion through various programs in the Commerce Dept., the S.B.A. and other government agencies.

The Small Business Export Expansion Act of 1980 directs the S.B.A. to provide educational and marketing assistance, and to improve access to export information and assistance for small business. In addition, the S.B.A. is supposed to establish the office of International Trade. If this is true, the S.B.A. should take the initiative to let small business know of these services and play the role of an information agency for those small businesses who are desirous of pursuing export activities.

2. The Department of Commerce

This department is also an information distribution dept. on foreign trade. Through the continued pleas of Commerce Secretary Malcom Baldridge, he prevented an O.M.B. 75% slash of funds which could have virtually terminated the Foreign Commercial Service, which aids trade abroad. The O.M.B. also proposed ending the Commerce Department's Office of Export Development and the Bureau of Industrial Economics. These funds must be left in tact if small business expects any assistance. The Commerce Dept. estimates more than $250 billion in export sales over the next 10 years has resulted from their efforts. Most of these sales go to big business. The same effort should be put forth on behalf of small business.

The Department of Commerce also assists businesses in exhibiting in foreign trade fairs. The participants run about 50%-50% for large and small business.

3. Foreign Joint Venture Information

Foreign joint ventures will become a necessity for U.S. business survival as discussed above.

The U.S. Government apparently has no program or source of information on joint ventures for the protection of American business. Private sources make some information available for a fee, such as Singapore being the safest place for a business investment within the next 5 years.

It is recognized that East and South Asia will be the low cost direct labor source for the 1980's and 1990's. Many of our exportable products will have to contain a blend of imported low cost labor combined with our technology to keep us in a worldwide competitive position. American business, and especially small business, must make foreign joint venture relationships before European companies establish such relationships. Many foreign nations have restrictions on how many companies they franchise or issue permits in a specific type of industry. Therefore the first to establish joint ventures will have the advantage.

It would be very helpful if our Government recognized the eventual necessity of foreign joint ventures and began to prepare informational data of the requisites on American companies imposed by each of the most popular joint venture countries such as S. Korea, Taiwan, the Phillipines, Indonesia, and Singapore. In addition the U.S. and these countries should execute reciprocal agreements of understanding for tariffs, free zones, investment protection, re-patriation of investments and compatibility law for U.S. firms. Such agreements

at this time would establish a precident for American business joint ventures prior to the inevitable rush from other nations.

B. GOVERNMENT COOPERATION IN THE EXPORT PROCESS

About one-hundredth of one percent of the U.S. Federal budget is spent for export promotion. Other major trading nations average six times this amount. Of the U.S. expenditure, there is no amount stated for the export promotion of small business.

Reagan Administration officials state that exporting is vital for America's economic recovery and acknowledge that more information needs to be directed toward small business to tap this large potential export resource; however, they hasten to add that they have few ideas on how to spur export sales.

It is recognized the U.S. has never had a clear export policy. Senator Jake Garn (R., Utah) says, "I think that for too long we have looked at exports as a privilege which the government grants".

Target areas, to compete with foreign competitors who receive aid in the form of direct loans, interest rate subsidies or preferential financing, are the Ex-Im Bank and the Export Trading Company Act.

1. Export-Import Bank

Constraints on the Ex-Im Bank must be reduced.

At a time when competitive financing is crucial for export competitiveness, Ex-Im Bank appears ill-prepared to aggressively support U.S. exports.

Legislation (to be introduced by John Heinz (R. Pa.) to give the bank more freedom to operate from the political constraints that now impede its performance should be supported.

With the strong interest to get Small Business into the Exporting Act, new legislation should contain a set-aside for small business so the bank's funds are not all alloted to big business.

2. Barter and Export Trading Companies

Small businesses without the resources to engage in all phases of the export process can benefit by working through a barter or export trading company.

Federal legislation before the Congress; Senate File 734, and House Files HR1648 and HR1799 speak to this issue. I urge you to pay close attention to this area of enormous potential for Small Business, and not allow this legislation to languish in committee any longer.

Since the bottleneck is in the Monopolies and Commercial Law Subcommittee of the House Judiciary Committee over the antitrust issue, they should be urged to mark up the Judiciary Committee draft of The Export Trading Company Bill and report it as soon as possible.

For additional information please refer to the attached "International Trade Policy" published by MACI (Minnesota Association of Commerce and Industry).

3. Education for an Export Mentality

Senator Rudy Boschwitz (R. Minn.) is one of seven experienced businessmen in the U.S. Senate. Because of his business experience it may be easier for him to recognize areas of actual business needs. For example, in a recent report on "Expanding Markets Abroad" Senator Boschwitz said, "What we need to do is develop an export mentality among small businesses and public officials alike". Development of this mentality needs to begin at the elementary school level.

John J. LaFalce (D. N.Y.) has co-sponsored a bill that would help states establish model foreign-language programs at the elementary and secondary school levels.

With a little guidance from Congress, maybe we can begin to teach Language, Culture and Customs along with Small Business and Entrepreneurship principals and practices in our schools. This would surely better prepare students entering the business world to immediately cope with foreign business.

Attached are two articles, one by Congressman La Falce and one by Albert Shapero of Ohio State University, which state this need in better terms than I could.

C. GOVERNMENT DEVELOPMENT OF STABLE LONG TERM, LONG RANGE PROGRAMS.

Briefly, our Government's on-again, off-again policies toward International business seem shortsighted and need a fresh look.

The Japanese have shown us how Government assistance in long range planning of financing, trade policies and government "Partnership" with the exporters have made them a world leader in exporting.

The time has come to document what our International presence or absence abroad means corporate-wise and personally, up-date American understanding of International risks and rewards, and support a new breed of Americans, especially Small Business to pursue the opportunities going by default outside the United States.

Following are a few points for consideration:

1. Small Business Export Loans

An incentive for Small Business to export would be through the availability of short term low interest loans available only on export sales.

Unlike domestic sales, foreign orders are generally shipped in one lot and not in scheduled partial shipments. This requires the use of more funds for a longer period of time. In addition, the foreign cycle of paying invoices can run 3 to 4 months from the billing date, due to business habits of foreign firms as well as the time necessary for payments to be processed through foreign, correspondent and domestic banking firms.

2. On-Sight Free Trade Zones

There has been much emphasis on moving business into Free Trade Zones to create employment in labor distressed areas. This subject is directed to large business who can set up a support facility to their overall business without having to move an entire business or operation.

For the benefit of Small Business an on-site Free Trade Zone for tax relief on inventory, direct labor costs and work-in-process for foreign destined sales would be an incentive for pursuing export business.

This benefit would probably necessitate a ruling from the I.R.S. permitting a separate set of books for tax purposes on inventory, labor and work-in-process in the on-site Free Trade Zone.

3. Update Government Information Toward International Trade

Changes in administration, policies, rules and regulations and foreign relations create a constantly changing turmoil that affects foreign trade.

Not only does exporting businesses need a current up-date, the stabilization of such information is necessary.

It is difficult and costly for business to make adjustments when political boycott or trade embargo is initiated against a foreign nation. In many instances an exporter has already committed funds or already produced merchandise which cannot be shipped. Our already depressed markets and cash short exporters cannot stand much more of this type of uncertainty.

Whether it is agricultural products or technological products a boycott or embargo diverts the anticipated sales of U.S. business to other supplier countries.

The Justice Department's proposed increased reward for information leading to convictions of offenders to $250,000 from $50,000 will create an influx of "Suspects" which increases the hesitancy for exporters to become involved.

4. GATT vs. Reciprocity Legislation

The General Agreement on Tariffs and Trade (GATT) and reciprocity legislation are two policies which the U.S. seems to be "Muddling through". Another case of not knowing where we are or what we will have to deal with.

To my knowledge, nothing has been incorporated into discussions which addresses Small Business interests. Could it be possible that the U.S. may gain the interest and cooperation of adverse foreign response by treating U.S. small business and foreign small business interest in equal relationship? After all foreign governments are as interested in promoting their small business as we are; however, when foreign governments look at U.S. competition, all they can see is our big business united front facing them.

5. Foreign Corrupt Practices Act.

The FCPA is presently a trade barrier to U.S. exports.

By now every businessman and legislator knows the need for revision and clarification in the accounting and anti-bribery provisions of this act.

The Chaffee Amendment, S-708, passed the Senate. The House of Representatives now has this important piece of legislation hung up on political issues. This kind of irresponsible selfishness is hurting our export ability at a critical economic time. All avenues should be explored to break this loose.

6. DISCs (Domestic International Sales Corporations):

The DISC should be retained and/or expanded. This has been a very useful tax treatment for small business who do export.

Good testimony to the importance of the DISC to a local Minneapolis business cannot be better told than by the commentary of Willis K. Drake, Board Chairman of Data Card Corp. A copy of Mr. Drake's letters are attached and give graphic proof of how a small business, now becoming a significant medium size business, has benefitted by the DISC program.

CONCLUSION:

Now that we have a foreign trade mentality growing in Congress, in Government departments and in the small business community, everything possible should be done to push export promotion.

The natural evolution of Small Business looking beyond domestic markets to foreign markets is following the same pattern as personal interests to travel and vacation abroad. Communications and transportation have brought distant places and markets as close as domestic markets were three decades ago. Unfortunately, our Government has not made the same progress in export support because of political leverage and prejudices at home and between foreign nations.

Present and future legislation for foreign trade must consider Small Business as a separate entity from big business. This has never been a consideration previously.

The above commentary is only the tip of an iceberg. With Small Business in its infancy in export promotion, now is the time to "Put on the small business cap" and think how all future legislation, policies, trade agreements, etc. will benefit or hinder small business exporting. With a common interest and purpose, there is no reason why small business will not take advantage of the opportunities offered to them.

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INTERNATIONAL TRADE POLICY

by Kel Johnson

The policy positions listed in this document were approved by the MACI Executive Committee on March 27, 1981. The policy statements do not touch every aspect of international trade, but they try to provide a meaningful direction for activity by our association.

An international trade questionnaire was mailed to the MACI membership as part of the "Minnesota's Business" publication in December 1980. The results were compiled and the MACI International Trade Committee met on several occasions and recommended MACI involvement in the areas listed. The trade committee consists of representatives from 85 MACI companies. For more information contact Kel Johnson, vice president for administration, 200 Hanover Building, 480 Cedar Street, Saint Paul, Minnesota 55101. (612) 292-4660.

MACI EXPORT POLICY STATEMENT

United States exports have contributed over $200 billion to the GNP and one out of every eight jobs in the manufacturing sector of the economy. In 1977, Minnesota exported $1.6 billion worth of manufactured goods while 35,000 jobs were dependent on exports of manufactured goods or one out of every nine manufacturing jobs in the state. Minnesota's share of U.S. agricultural exports totaled $918 million in FY 1977 where one out of every $4.00 came from exports. But, the U.S. share of world exports has been declining since the mid-1960's and the U.S. trade deficit for both 1978 and 1979 was in excess of $30 billion. The United States barely exports 7% of its GNP and only 8% of the nation's 300,000 manufacturers export (fewer than 200 companies) accounting for more than 80% of the U. S. manufactured exports.

The United States government has given international trade a low priority for many years. Because of this lack of interest, efforts to expand exports have been impeded by disincentives, ranging from the adverse consequences of regulation to ineffective government. Commercial policies of the major industrial countries maintain fewer disincentives than the United States. The United States needs to develop an overall export trade orientation. Increased exports would contribute not only to a more favorable balance of trade for the United States, but also would result in a stronger economy and more jobs. To reach this objective, existing governmental disincentives should be eliminated—occurring in the areas of ineffective government organization, taxes, a vagueness of the Foreign Corrupt Practices Act, detrimental consequences of regulations, slow export licensing procedures, and anti-trust laws unnecessarily restricted in foreign markets.

To establish an export expansion target, the MACI International Trade Committee recommends the following legislative policies necessary to achieve this goal:

EXPORT TRADING COMPANIES

MACI POLICY

Support legislation to facilitate the formation of "one stop" export trading companies including authorization for equity participation by banks, clear and meaningful anti-trust exemption, allow for DISC participation.

BACKGROUND

The purpose of the trading company concept is designed to encourage the formation of export trading companies to link potential U.S. exporters with overseas markets. Trading companies have existed in the United States in various forms. So, legislation is not needed to authorize trading companies. But, in the past, trading companies in the United States have stayed relatively small and very specialized and have been restricted because of limitations of financial resources. The reason behind the proposed legislation in Congress is to provide benefits and incentives which would induce the creation of U. S. trading companies that can be organized and operated as "one stop" trading facilities capable of providing documentation, distribution services, market analysis, freight forwarding, financing and follow through. Revisions of the Webb-Pomerene Act of 1918 is needed to clarify the anti-trust provisions applicable to export trading associations and to provide a certification procedure enabling export trade companies and other such associations to receive anti-trust clearance for export trade activities. Anti-trust laws find their justification in promoting a desired level of competition within the domestic economy.

However, their application extraterritorially often produces a sole result of lessening the U.S. exporters competitiveness in foreign markets. Legislative proposals in Congress dealing with export trading companies and export associations address existing deficiencies in the anti-trust exemption in three key areas. First, the anti-trust exemption would become applicable to the service sector, from which approximately 65% of the GNP is derived and which presently accounts for about 70% of the domestic employment. Second, the legislation would create a more realistic standard of eligibility to qualify for the anti-trust exemption. Third, create specified certification procedures for the purpose of assuring the business community that cooperative export activities will not later become subject to anti-trust liability.

The most controversial item with the proposed legislation would eliminate some of the existing prohibitions against banking involvement in commercial activity by allowing limited investment by U.S. banks and export trading companies. Among the reasons given for maintaining the traditional distinctions are:

(1) Banks should focus on loans and deposits and can better exercise independent judgement on whether or not to make a loan if they are prohibited from holding a stake in the management;
(2) Banks could be exposed to unfamiliar and excessive risks in commercial trading and the holding of inventories;
(3) Bank regulatory agencies lack the capacity to evaluate the commercial risks banks would encounter in owning export trading companies; and
(4) Bank capital is low and should be reserved for support of bank loans.

Among the reasons for investments by U.S. banking institutions are:

(1) Banks bring assets, supporting facilities and services which U. S. exporters now lack by contrast with competitors;
(2) Banks can encourage and help exporters develop a longer term view of and presence in the market;
(3) Bank-affiliated trading companies would have special effect on encouraging more medium and small exporters who are now discouraged by the remoteness and strangeness of foreign markets and buyers exchange risks, and the complexity and expense of documentation;
(4) Banks have international offices, experience in trade financing business contracts abroad, international marketing knowledge, and familiarity with domestic U.S. producers.

DISC (Domestic International Sales Corporation) provisions of the tax code extended to all export trading companies would have two purposes: (1) to enable export trading companies to use DISC with respect to all their income from exports of services as well as products; and (2) to permit small, closely held companies to pass through net losses in the first few years when start-up costs are likely to exceed income.

The U.S. Treasury Department computed the estimated potential revenue cost of extending DISC benefits at $200 million per year.

TAXES

MACI POLICY

Support substantial changes in the tax code to reduce the tax consequences of Americans working overseas.

BACKGROUND

Under present income tax law, Americans working abroad are on a significantly less favorable tax footing than citizens from competing industrial nations. The United States is the only major industrial country which taxes the earnings income of its citizens serving abroad, who are also subject to foreign income taxes in the country to which assigned. This has often resulted in increased labor costs substantially, and has forced some U.S. companies to replace their employees abroad with foreign workers. An exclusion of foreign source earnings was part of the U.S. Tax Laws Section 911 until 1953 when Congress adopted a $20,000 ceiling for citizens physically present abroad for seventeen out of eighteen months. In 1962, Congress put a $20,000 limit on earned income for the first three years of residence and citizens living abroad for more than three consecutive years became subject to a $35,000 limitation. In 1964, Congress changed the $35,000 exclusion to $25,000. In 1978, Congress passed into law a new Section 911 for taxing Americans working abroad. The new law allowed a limit of $20,000 for employees in the following two areas: (1) employees working for charitable organizations working in developing countries; (2) employees required to live in camps because of inadequate housing. Other U.S. citizens were given special deductions in the following areas: housing, education, moving expenses, sales or exchange of residency, cost-of-living, $5,000 deduction for hardship areas, and home leave.

MACI POLICY

Congress should retain and broaden the tax deferral options of the Domestic International Sales Corporation (DISC), allow export trading company participation, and increase the 100% exemption clause to $500,000.

BACKGROUND

DISC was adopted under the Revenue Act of 1971 as a device to assist U.S. exporters by granting domestic exporters tax benefits comparable to those received in other countries, offsetting incentives for U.S. companies to locate or to expand manufacturing abroad. A DISC is a domestic corporation usually established by an affiliate

with a domestic producer, which is typically the parent company within the United States. The DISC can operate as a principal, buying and selling for its own account, or as a commission agent. The law allows a manufacturer to set up a separate DISC vehicle that pays no taxes on export income up to $100,000 and can defer taxes indefinitely on 50% of income above that amount. According to the U.S. Treasury Department, approximately 60-70% of all manufacturers that export use the DISC. The cost per year for all U.S. businesses participating under the DISC program is running approximately $1.2 billion or one percent of the total gross export dollars. A DISC is a domestic corporation that meets the following requirements:

- Has at least $2,500 paid-in capital.
- Has only one class of stock.
- Files a statement of election to be treated as a DISC with the Internal Revenue Service.
- Demonstrates shareholder consent to such election.
- Maintains its own bank account and accounting records.
- At least 95 percent of its income must be from qualified export receipts.
- At least 95 percent of its assets must be export related.

The tax-deferred earnings retained by the DISC can be:

- Invested in its export business—to build up inventory of products to be exported or to provide office and warehouse facilities and other property
- Used to extend financing to its foreign customers.
- Invested in certain Export-Import Bank, obligations or in "producer's loans" to related or unrelated U.S. producers for export, to help improve their production capacity, or to develop new products.

The White House Conference on Small Business recommended that Congress allow American trading companies participation in the DISC and an increase from the $100,000 exemption clause to $500,000.

EXPORT LICENSE APPLICATIONS AND SHIPPERS EXPORT DECLARATIONS

MACI POLICY

Support continued confidentiality of export license applications and shippers export declarations and communications between U.S. exporters and the government which contain vital and proprietary business data.

BACKGROUND

The Export Administration Act of 1969 protects the confidentiality of information submitted to the Department of Commerce regarding exports. The act provides that no information obtained under the act which is deemed confidential is to be made public unless the Secretary of Commerce determines that withholding it is contrary to the national interest. At the present time, existing federal law and regulations require U.S. exporters to include sensitive information in export license applications and file shippers export declarations for each merchandise shipment in excess of $500 when it is shipped from the United States. During 1978, The New York Journal of Commerce (Twin Coast Newspapers, Inc.) requested access to individual SED's under the Freedom of Information Act. When denied access by the Census Bureau and the U.S. Department of Commerce, Twin Coast filed suit in federal courts to compel disclosure. Twin Coast argued that the government's reason for justifying confidential treatment for such business data were inadequate to satisfy the criteria for exemptions under the Freedom of Information Act. Because of the pending court case, Congress passed into law H.R. 6842 (Public Law 96-272) which clarified the confidentiality of export license applications and provided for continued confidentiality of shippers export declarations and communications.

MACI POLICY

Develop a specific license procedure within the U.S. Department of Commerce (Office of Export Administration) which is both efficient and effective with the flow of trade between the United States and foreign markets.

BACKGROUND

Regulation in this area is of significant direct cost, both in loss of business and internal administrative expense. Problems arise through provisions of the Export Administration Act and the regulations and practices of the U.S. Department of Commerce.

Two major problems—a long delay in processing requests and waivering government policies regarding U.S. trade with certain nations. Those factors leave some foreign customers to regard U.S. businesses as unreliable sources of products and services. Long delays in the processing of license requests are responsible for a loss of sales. License applications must often go through several government departments before they can be approved. The reason for the delay is personnel shortages in the Commerce Department. New regulations in place as of July 1, 1980, set limits on the time it should take Commerce to issue a license. At the present time, there is no strong evidence of change.

FINANCING

MACI POLICY

The EXIM Bank lending authorization should be increased.

MACI POLICY

The EXIM Bank should be treated as a separate line item by removing it from the Foreign Assistance Appropriations Act.

BACKGROUND

The Export-Import Bank (EXIM Bank) was founded in 1934, as an independent corporate agency of the U.S. government. The bank is managed by a board of directors, including five full-time directors appointed by the president and confirmed by the Senate. Its function is to assist in financing the export trade of the United States. The EXIM Bank is directed by statutes to (1) offer financing that is competitive with that offered exporters by other countries by their official export credit institutions, (2) determine that the transaction supported provides for a reasonable assurance of repayment, (3) supplement, but not compete with private sources of export financing, and (4) take into account the effect of its activities on small business, the domestic economy, and U.S. employment.

The EXIM Bank extends direct credits to borrowers outside the United States, export credit insurance, and export credit guarantees. Long-term direct credits to foreign borrowers are usually extended in connection with sales abroad of capital goods. EXIM Bank will finance a portion of the U.S. costs with the balance of the financing provided from the borrowers' own resources and private resources. EXIM Bank may guarantee part or all of the private financing. Assistance is limited to transactions supporting export only from the United States.

The EXIM Bank receives neither an annual appropriation nor does it directly use taxpayers' dollars. Its borrowings, which are arranged through the Federal Financing Bank in the U.S. Treasury, have a lower rate of interest than if they were raised by a private institution. This allows financing of U.S. exports at rates more nearly competitive with products of other countries. Even though the bank does not receive an annual appropriation, its lending is limited by congressionally imposed annual authorization ceilings.

At the present time, the annual authorization for EXIM Bank is a line item that is part of the Foreign Assistance Appropriations Act within the federal budget. It is, therefore, subject to a reduction as part of the overall budget cuts of the current administration.

The bank is authorized to have outstanding at any one time dollar loans, guarantees, and insurance in aggregated amounts not in excess of $40 billion. The volume of exports supported by EXIM Bank in 1973 was $10.5 billion, direct credits were $2.4 billion, discount program advance commitments were $1.6 billion and financial guarantees were $1.5 billion. In 1977, the bank extended direct credit of only $700 million, below its lending authority. In 1979, its full $3.6 billion direct loan authorization was used. In 1980, the bank exhausted its credit authority before the fiscal year was completed. At the present time, the bank is authorized to have capital stock of $1 billion and to borrow from the United States Treasury up to $6 billion outstanding at any one time. Since 1934, EXIM Bank has authorized direct loans of $30.6 billion with a total net write-off of only $3.7 million. EXIM Bank has supported through its programs more than $100 billion in U.S. export sales, and has paid more than $1 billion in dividends to the U.S. Treasury.

Summary of EXIM Bank programs.

Direct loans and financial guarantees.
EXIM Bank facilitates exports of major capital equipment, requiring the repayment terms over five years, through direct loans to foreign buyers for a portion of the required financing. Commercial banks generally provide the remainder of the financing. While the loans are extended to the foreign buyers, the funds never leave the United States because they are paid to the U.S. exporters. The foreign borrowers repay the loans, plus interest and other fees to EXIM Bank and the private lenders.

Commercial bank guarantees.
EXIM Bank guarantees the repayment of medium-term (181 days to five years) export credit extended by U.S. banks to foreign buyers, without recourse to the U.S. exporters. The commercial bank retains a share of the commercial risk for its own account, and is protected by the EXIM Bank guarantee against the remaining commercial and political risk. During 1979, EXIM Bank authorized 573 bank guarantees totaling $399.2 million.

Discount loans.
EXIM Bank provides stand-by assurance to U.S. commerical banks which purchase fixed rate export obligations. Advanced commitment to discount a note must be approved by EXIM before the covered exports are shipped. Once the commitment is received and before the note is repaid, the bank may borrow from EXIM up to the

remaining value of the obligation. This program is intended to overcome limitations in the private market's willingness to provide medium-term (272 days to five years) fixed-rate financing for export sales. In 1979, EXIM authorized 753 discount loan commitments totaling $60 million.

Cooperative financing facility.
EXIM Bank enters into agreement with overseas financial institutions to lend them funds on terms of one to five years which they in turn re-lend to cover one-half of the financing for a particular U.S. export. The foreign bank provides the other half of the funds and takes the credit risk on the entire transaction. This program supports small and medium sized U.S. export sales by assisting foreign buyers, who because of size, inexperience, or other factors are unable to obtain credit to finance their purchases through the U.S. private sector or other EXIM bank programs. EXIM approved 468 CFF loans for a total of $122 million and 233 financial guarantees relating to CFF loans totaling $26.1 million in 1979.

FCIA export credit insurance.
The Foreign Credit Insurance Association (FCIA), an association of commercial insurance companies formed by EXIM Bank and the insurance industry, provides credit protection for all sizes of exporters. EXIM Bank insures short-term (up to 180 days) and medium-term (181 days to 5 years) export credit provided by the private sector. FCIA provides insurance coverage against defined commercial risk, while EXIM Bank provides political risk coverage and re-insures FCIA against excessive commercial losses. The program spreads the risk in export credit among the exporter, FCIA, and EXIM Bank in accordance with classic insurance principles, thereby enabling exporters to sell abroad and the private market to provide the needed financing. EXIM authorized 2,315 FCIA insurance transactions during 1979 totaling $4.1 billion, in support of $5.9 billion in U.S. exports.

Reduction of EXIM Bank Direct Lending.

In accordance with President Reagan's cutbacks in federal programs, the administration is proposing that the EXIM Bank's authority to make new direct loans be set at $4.4 billion in 1982, down 31% from the current base. The administration's proposal would be less generous and credit would be more carefully targeted. Promoters of extending the export EXIM Bank's lending authority feel that the bank has been used as a vehicle for head-to-head competition with foreign export subsidy programs, and argue that further growth in the EXIM Bank's direct loans is necessary to expand export, reduce U.S. trade deficits, and halt the declining U.S. share of world trade.

FOREIGN CORRUPT PRACTICES ACT

MACI POLICY

The President of the United States should negotiate an International Code of Business Conduct Treaty among the industrialized and developing countries, with whom the U.S. competes in the international marketplace. When the treaty has been signed, the "Foreign Corrupt Practices Act" should be repealed. Until such a treaty is in place, Congress should immediately replace or further clarify the ambiguities of the act.

BACKGROUND

The Foreign Corrupt Practices Act (FCPA) was signed into law in 1977. The law makes it unlawful for U.S. firms (stockholders, directors, officers, employees, or agents when acting on behalf of their firms), directly or indirectly, to bribe any foreign government official, political party or party official, and candidates for political office for the purpose of obtaining or maintaining business. The law as passed had an exclusion which provided that the term "foreign official" means any officer or employee of a foreign government or any departmental agency acting in an official capacity on behalf of any government or department or agency. The act requires firms with securities registered with the Securities and Exchange Commission to keep detailed books, records, and accounts which accurately reflect the disposition of the firms' assets. The firms are required to institute and maintain internal accounting control systems to assure management control authority and responsibility over the firms' assets. Two federal agencies are involved in the enforcement and administration of the Act. The record keeping and accounting controls provisions of the Act, requiring accurate accounting of corporate transactions and expenditures with respect to payments made overseas, are under the authority of the Securities and Exchange Commission. The criminal penalties for corporate "bribery" of foreign officials is under the Department of Justice. Because of the perceived ambiguities in the law and resulting uncertainties as to its enforcement by the Department of Justice and the Securities and Exchange Commission, the law has provided a disincentive for exporter.

PORT OF DULUTH

MACI POLICY

Support the Seaway Port Authority's request for state general obligation bonding for part of the public marine terminal modernization and expansion program.

BACKGROUND

The Seaway Port authority of Duluth was established by the legislature in 1955. The port authority is charged with the duty of promoting the general welfare of the port district, increase the volume of commerce through the port, and promote the safe and economic handling of such commerce. Construction of the Arthur M. Clure Public Marine and Terminal in Duluth was authorized by the state legislature in 1957, two years before the scheduled opening of the St. Lawrence Seaway.

The legislature authorized the appropriation of $10 million to be provided as follows: $5 million from the State of Minnesota, $4 million from the County of St. Louis, $1 million from the City of Duluth. A 120-acre parcel of property, most of it submerged under the waters of the St. Louis River Bay, was designated as the site. The main construction was completed in time for the 1959 seaway opening and 90% of the project was completed by 1961. Public bonds issued to finance the original project were retired by 1979. A container crane facility and related dockside improvements totaling $2.25 million were completed in 1975 through a City of Duluth bond issue, two grants from the Economic Development Administration and Port Authority funds. Other lesser improvements, maintenance projects and equipment acquisitions costing nearly $600,000 have been realized through direct expenditures of port authority funds.

In order to accommodate the new generation of ships and cargoes plying the seaway, an area has been designated to become a multi-purpose dock serving two 200 ton mobile cranes, a 90,000 square foot warehouse and an open storage yard. Development of the multi-purpose dock would enable the Port of Duluth to handle a wide variety of cargoes it presently cannot accommodate and would result in a significant increase of jobs for longshoremen, warehousemen, pilots, tugmen, line handlers, ship chandlers, agents, forwarders, inspectors and others engaged in the maritime transportation industry.

The Port Authority Board of Commissioners has unanimously approved a recommendation to seek $7,600,000 in public funds for the expansion project. Governor Quie announced that he was recommending $2.5 million in state bonds for the expansion and renewal of the port. The participation is contingent on the securing of federal and local funds. The $2.5 million will be part of Quie's bonding bill to be introduced in early April.

MACI POLICY

Support the Seaway Port Authority's request for funds for the purpose of worldwide promotion of the port.

BACKGROUND

Since 1963, the port authority has received state funds earmarked strictly for the purposes of promotion and trade development. Initial appropriation in 1963 was for $55,000 annually when the total administrative promotion budget was $121,848 for the port authority. The present appropriation is for $90,000 annually when the total administrative-promotion budget is in the area of $500,500. During the 1981 and 1982 legislative session, the Seaway Port Authority is seeking $150,000 for the first year and $200,000 for the second year. (Governor Al Quie has recommended $100,000 for the first year and $100,000 for the second year.) Proposed expenditures for promotion and trade development is $333,500 for the year ending March 31, 1982, and $438,000 for the year ending March 31, 1983. (the port authority's fiscal year runs from April 1 to March 31.)

The objectives of the International Trade Development Program for the port are as follows:

1. To introduce potential port users to the port's capabilities in areas where the port is not known.
2. To aid Minnesota firms, new to international trade, on the mechanics and benefits of increasing exports.
3. To seek transportation rates that will provide Minnesota farmers and manufacturers with a competitive advantage in the markets of the world.
4. To increase awareness in the international community about Minnesota's World Port, our state, and the advantages of doing business with both.
5. To stimulate use of the port by exporters, importers, steamship companies and others not now using the port.
6. To promote continued and expanded use of the port by exporters, importers and steamship companies and others already using the port.
7. To build further public awareness and interest in port activities at community, state and regional levels.
8. To foster harmonious relationships among the various port interests for the collective good of the port.

Poor Foreign-Language Skills Are Hurting U.S. Business

By John J. LaFalce (D-N.Y.)

When General Motors advertised its "body by Fisher" car in Belgium, the slogan was described in Flemish as "corpse by Fisher." In Spanish-speaking countries, car buyers avoid the Chevrolet Nova because "No va" in Spanish means "It doesn't go."

These are anecdotes about foreign trade that shed a little humor on an otherwise sobering situation.

Children Tongue-Tied

The United States prides itself on being the "melting pot" for a multitude of the world's people. Yet, our people — especially our children — are increasingly tongue-tied when they face foreign languages.

From the executive suite to the halls of government, we are becoming a people unable to communicate in the language of our neighbors.

Only 15 percent of U.S. high school students take a second language, and just 5 percent pursue foreign languages for more than two years.

The situation is barely better at the university level. In 1966, 34 percent of all colleges required a foreign language for admission, but now only 8 percent have such a requirement.

Our inability to communicate effectively has resulted in our slippage in the ongoing battle to maintain both our military and economic superiority.

The ripple effect of this poor training finds its way into the most sensitive areas. The U.S. State Department, our primary link with foreign nations, no longer requires a Foreign Service candidate to have any knowledge of a second language.

Intelligence leaders continue to complain that there is a shortage of skilled translators and linguists fluent enough to understand the colloquial, idiomatic and special regional and slang terms used abroad.

This condition has led CIA Deputy Director Bobby R. Inman to complain, "The deteriorating language-study capabilities programs of this country are presenting a major hazard to national security."

In the business community, this problem is especially aggravating. One recent study estimated there were 10,000 English-speaking Japanese sales representatives in the United States, while fewer than 900 Americans were in Japan, and only a handful of those persons actually spoke Japanese.

Japanese trade officials emphasize they make a special effort to train their business executives in the language, culture and customs of many foreign people to enhance their ability to conduct foreign trade.

Is it any wonder this tiny nation is so powerful in the world of imports and exports?

The humorous but nonetheless serious situation General Motors confronted in its advertising campaigns is all too prevalent in the efforts of American firms to expand abroad.

LaFalce

Fortunately, the problem is getting a bit more attention in corporate board rooms across the country.

PepsiCo International Vice President Edmund B. Piccolino has commented, "Every day we face situations where the lack of foreign language training on the part of our international cadre of executives restricts their ability to move and grow in their careers, increases our costs to do business and impairs our ability to do business around the world."

The dearth of foreign-language training is not an isolated problem; it afflicts schools, corporations and businesses across our nation.

Guidance May Be Needed

A little guidance from Congress may be what is needed if the United States is to become more fluent.

I've co-sponsored a bill that would help states establish model foreign-language programs at the elementary and secondary level.

The legislation would also encourage college foreign-language study by awarding grants to schools based on their foreign-language course enrollments.

This is only a first step. The major impetus for change must come on the local level, where the control of our schools resides.

I hope that local and state officials begin to take action on this front. Our inability to understand foreign tongues is becoming a serious problem that deserves immediate attention.

SPEAKING OUT

ARE BUSINESS SCHOOLS TEACHING BUSINESS?

More students want to be entrepreneurs, but their professors are turning them into bureaucrats.

By Albert Shapero

There are virtually no colleges of business in the United States today; there are only academies of bureaucratic middle management. The 1,180 institutions granting degrees in business and management teach how to fit into and serve the 5,000 largest corporations. The concepts and values taught are those of the corporate bureaucrat or staff professional. Although the typical M.B.A. might vote for a conservative political ticket, his training has prepared him to work equally well in the Department of Energy, General Motors, or a Soviet commissariat.

There has recently been a flurry of criticism of the dedication of M.B.A.s to "fast-trackism" (getting to the top without ever making or selling anything). But nothing has been said of business schools' lack of interest in and even contempt for small business and entrepreneurship. It may seem difficult to reconcile our national decline in productivity with the growth in the number of M.B.A.s, but the relationship between the two phenomena becomes clear when we note that our institutions of business education essentially ignore the 14.1 million businesses that are "small" by the Small Business Administration's standards, and that these businesses account for 58% of U.S. employment and for the majority of new jobs and innovations.

Small business and entrepreneurship are practically invisible in the curriculum and the textbooks of so-called schools of business administration. Most schools offer one or two courses in small business, but they are never required and are usually taught by outsiders or professors who have given up all hope of promotion.

The ignorance of small business in higher education also shows up in the textbooks used in other courses. Over 1,000 schools, primarily community colleges, offer a first course in the business curriculum with a title like "Introduction to Business." It is the course that gives the entering student a first notion of business from the academic viewpoint. The course provides one of the most lucrative textbook markets, hotly contested by textbook publishers who spend lots of money to develop and market what they think faculty members want. The books are large and elaborately illustrated in color, and the faculty are provided with extensive teaching aids.

"What do you mean this is the section on small business?"

Of five leading textbooks I've analyzed, only one has a chapter devoted to small business and a very short chapter at that (23 of 621 pages). A count of the cases, examples, discussion questions, and references in the five books showed 85% to be concerned with large corporations. There was far more discussion of government concerns in "Introduction to Business" texts than there was of small business.

The emphasis doesn't change when we examine the textbooks used in other fields: organizational behavior, management science, production, marketing, advertising, personnel, and microeconomics. Well over 80% of the examples, cases, and problems have to do with very large corporations; Du Pont, General Motors, General Electric, and IBM are mentioned several times in each book. When small business is referred to, it is usually with phrases like "small firms tend to be weak and short-lived," or "small business careers are poorly paid, and there is a high failure rate." Often, examples of small business are simply cute: They have names like Mandy's Massage Parlor or Ptomaine Gulch Restaurant.

Almost everything in the academic reward system discourages the faculty from interest in small business or entrepreneurship. It's true that jobs for Ph.D.s who did dissertations on small business are almost guaranteed. Students like the few small business courses that exist, so there is a demand for teachers who can teach more of them.

But one can almost guarantee that once a small business specialist is hired, he will never be promoted. Publishing in respected academic journals is fundamental to academic promotion, and the journals refer each submission anonymously to other professors for judgment. Between 1975 and 1979 no "respected" academic journal published as many as five articles on small business and entrepreneurship. But at the same time, the public's interest in entrepreneurship was increasing: The number of articles on small business in popular periodicals doubled during the same period.

So why should any academic do research on small business or entrepreneurship? It won't be published where it counts. And it isn't likely to produce lucrative consulting contracts.

The mainstream of academic research is concerned with theory and mathematical model building. Where can you use a mathematically interesting theory in a company that has only one person who simultaneously serves as chief executive, production manager, sales manager, finance direc-

Albert Shapero, an academic himself, is William H. Davis Professor of the American Free Enterprise System at Ohio State University.

SPEAKING OUT *(from page 13)*

tor, accountant, and shipping clerk? What kind of OD (organizational development) or MBO (management by objectives) program is appropriate to the four-person business? (A majority of U.S. businesses have fewer than four persons in them.) How can you sell a retreat on Megabuck Island to a business like that? It is easy to see, if not to agree with, the point of view of most academics.

Beyond the immediate problems of publishing in the proper journals and finding consulting jobs, there is a more profound and pervasive basis for the business schools' lack of interest in small business. Business administration faculties are part of a larger intellectual and cultural milieu, centuries old, that holds commerce in contempt. It barely tolerates corporate executives. It despises small businessmen. A recent study by The Media Institute viewed a sample of 200 episodes of popular TV programs and found that heads of big businesses were shown to behave illegally 75% of the time, malevolently 10% of the time, but never foolishly. Owners of small businesses were depicted as acting foolishly 43% of the time, illegally 30% of the time, and malevolently only 10% of the time.

A friend told me of a speech given by one of Harvard's distinguished academics to incoming freshmen. To illustrate what one should never aspire to, he quoted a New England epitaph that reads, "Born a Man. Died a Grocer." No intellectual would like to think of Henry David Thoreau running a grocery store or selling pencils, though in reality Thoreau's father owned a pencil-manufacturing business. A civil engineer by training, Henry introduced several innovations that made the business profitable and represented the business when he traveled. But few intellectuals know or care that Thoreau was deeply involved with small business.

Today, the children, taxes, and alumni fund contributions of small businesspeople are crucial to the sustenance of our institutions of higher learning, but small businesspeople get little in return. Their children are socialized and prepared for a place in some large bureaucracy—if not a corporate one then a governmental one. Their financial support is used for research relevant only to the very largest of organizations. No one is studying the dynamics of partnerships, for example, figuring out how to make them work. Where is the research relevant to new and small businesses? Small business is likely to remain invisible in academe. □

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DATA CARD CORPORATION

W K. DRAKE
Chairman of the Board

RECEIVED
APR 7 1982

April 2, 1982

Mr. Glen M. Stout
Chairman of the Board
The Maxi-Switch Co.
9697 East River Road
Minneapolis, MN 55433

Dear Mr. Stout:

I recently mailed the enclosed letter to Treasury Secretary Donald T. Regan.

I am sure you are aware of the efforts by some Treasury officials to modify the Domestic International Sale Corporation (DISC) program. I fear that the story of how well the provisions worked for those companies aggressively marketing in the export area will be dismissed by Treasury officials as being atypical.

The impact of DISC on Data Card is not an unusual example. Many companies in our area have been similarly impacted.

I hope you will support the efforts to maintain the DISC program as it is currently structured and will communicate this position to the Secretary of the Treasury.

Sincerely,

W. K. Drake

W. K. Drake
Chairman of the Board

Enclosure

11111 BREN ROAD WEST • P.O. BOX 9355 • MINNEAPOLIS, MN 55440 • 612 / 933-1223

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DATA CARD
CORPORATION

April 1, 1982

Mr. Donald T. Regan
Secretary of Treasury
15th & Pennsylvania Ave., N.W.
Washington, D. C. 20220

Dear Mr. Secretary:

I am writing to earnestly request that you do not support the reported plans of the U. S. Treasury Department to seek a repeal of the Domestic International Sales Corporations (DISC) program.

Please let me briefly cite my reasons.

I am the board chairman of Data Card Corporation, a manufacturer and marketer of a line of high technology machines for business and industry including: equipment to emboss and encode plastic cards; specialized magnetic ink character (MICR) printing equipment; electronic weighing equipment; and automated laser machining systems. Our company was founded in 1969, and we have been a participant in the DISC program almost since that program was started in 1972.

The DISC program, as you know, allows participating companies to defer a portion of their tax liability on earnings from the sale of their goods abroad. As a practical matter, these deferred tax monies become increased working capital for the companies involved, which they can use to strengthen their export manufacture and sales operations. The overall goal is a steadily increasing volume of export sales for the United States, with the increased employment of Americans to make export goods, and the favorable trade balance-of-payment effects that inevitably result.

In the nine years Data Card has been a DISC participant, the total tax deferred monies involved for our company -- i.e., the increased working capital available to us over these years -- has been $4,165,000. A result has been an across-the-board strengthening of our export program, to include the development of products specifically for the export market, and the aggressive merchandising of these products.

The results, Mr. Secretary, have been impressive.

In our first year of DISC participation, our fiscal 1973 year, our company had only $526,000 in export sales, out of total sales of $4,832,000.

By 1976, three years later, export sales had climbed to $2,401,000, out of total sales of $14,553,000.

And in fiscal 1981, export sales were up again -- $9,904,000, out of total sales of $75,366,000.

The substantial gain in our export business over the years is obvious, as is, I believe, the fact that this has allowed Data Card to employ people it otherwise could not employ, while simultaneously contributing to an easing of the nation's balance-of-payment problems.

A key to all of this, Mr. Secretary, has been the DISC. Without DISC, Data Card would have had less working capital to expand its export program. We would not have been able to divert equivalent capital from our domestic program needs for this purpose. That's the way it is with young, growing companies like Data Card who are always in a "working capital crunch." In short, Data Card simply could not have developed as substantial in export program as it now has were it not for the DISC.

We keep hearing, Mr. Secretary, about government programs that "don't work." Well, here's one, the DISC program, that <u>does work</u>, and superbly so. Given the nation's unemployment and balance-of-payment problems -- and given the fact that DISC deals so effectively with these problems -- it is extremely difficult to understand why a repeal of DISC would be advocated. If the argument is that the Treasury is losing money because of DISC, that simply won't hold. The increased taxes generated by DISC-increased employment and business will far outweigh the taxes deferred under DISC.

While Treasury studies may cite a concentration of benefits among the larger companies as justification for the elimination of DISC, small companies like Data Card need this type of program to aggressively enter the export market. If smaller and mid-size companies are to realize their export potential, DISC must be maintained.

Again, Mr. Secretary, I earnestly ask that you not give your support to any DISC repeal attempt. Thank you very much for your consideration.

Sincerely yours,

W. K Drake

Willis K. Drake
Chairman

Senator DIXON. May I make this comment, Mr. Chairman? First, I want to say that I am very impressed by the presentation by Mr. Stout. It is extremely helpful. I want to make this observation. Several items that he touches upon in his remarks, as he has indicated, we have dealt with in the Senate. I am a member of the Banking Committee, as well as this committee. The Export Trading Company Act was marked up in the Banking Committee. Before I came here, it had been a bill originally sponsored by my predecessor, Senator Adlai Stevenson from Illinois. This past session it was sponsored principally by Senators Heinz and Danforth, with other cosponsors. It passed the Senate unanimously, but so far has not made much progress in the House.

In the Senate Banking Committee as well, we had the modification of the Foreign Corrupt Practices Act proposed by Senator Chafee. For a long time, that was extremely controversial. I happened to have been one on my side who was largely responsible for entering into some compromises in the committee, which ultimately gave us an opportunity to adopt the necessary modifications to that bill and pass it from committee. Ultimately, it was passed in the Senate unanimously.

Both of those pieces of legislation now pending in the House are fundamental to the central theme that Mr. Stout presents to us here. I would hope, Mr. Chairman, and Senator Weicker, that if they do not have a comparable advisory committee to this one in the House, someone is not telling our friends how significantly important members of the small business community in this country view these two pieces of legislation.

I would make one final comment. I was pleased to note your remark about the need for more education in other languages in our school system in our country. I do not know that I am ready to accept compulsory second language legislation at the elementary school level. But my good friend, Congressman Paul Simon, from the 24th Congressional District in Illinois, was my seatmate in the Illinois House and Senate before we both came to Congress. He has so often told a story about why the Japanese do so much better in this country than we do in theirs. We have a couple of people in Japan who speak fluent Japanese, and they have 1,000 salesmen in New York City alone who speak fluent English.

I think there is a message in that which the country ought to become more and more aware of. I thank Mr. Stout for enlarging upon that theme here. I think what he has said is extremely valuable.

My State is heavily dependent on agricultural exports. It used to be second, but now I am sorry to say third, but still important, in the export of manufactured goods. There is no more important thing for us to discuss, to turn this economy around in this country, than the very things you have discussed. I am pleased that you have presented it so well, and I would hope there is a message for our friends in the House. Sometimes I wonder if they hear the same things we hear, because I think these two pieces of legislation we passed unanimously in the Senate are the cornerstones of what we need to do in this area. I am just very sorry that more progress is not being made in the House.

Mr. MUDGE. Thank you. As one who testified in front of your committee on May 21 last year, I was very pleased to see that you, Senator Dodd and Senator Riegle did help us with removing that disincentive.

We are working now with the subcommittee in the House. We are promised hearings in June. There were to have been hearings on the matter in April, but I believe the leadership has rescheduled the subcommittee hearings from Monday to Friday because of the budget. We submitted language to them we think they can live with.

May I move on, Senator Nunn and Senator Weicker, in the interest of time? I would like to call on Bruce Hopewell to discuss Regulation 385, which perhaps is the most pernicious that has confronted venture capitalists and small businesses yet devised.

REPORT ON CAPITAL FORMATION/TAXES

Mr. HOPEWELL. I appreciate the opportunity to submit for your consideration comments on Regulation 385. The current version of the 385 regulation, dealing with debt versus equity, promulgated by the Department of the Treasury in January 1982, is scheduled to go into effect for corporate debt instruments issued after June 30, 1982.

This version is an improvement over Treasury's previous draft, promulgated in December 1980, in the sense that a number of the more obvious impediments to venture capital investing have been deleted or softened. However, the proposed regulations, if they go into effect as presently drafted, will constitute a significant impediment to the expeditious and orderly flow of venture capital needed to finance American small businesses.

No. 1, the proposed regulation contains rules explaining when corporate debt instruments will be treated as preferred stock rather than as debt for Federal income tax purposes. In this case: (*a*) Interest paid on such equitized debt instruments will not be deducted by the corporate payer because it will be treated as dividends on preferred stock; and (*b*) when the equitized debt instrument is ultimately redeemed by the corporation, the holder's proceeds may be taxed as a dividend under the complex existing rules of code No. 302, which taxes as a dividend any preferred stock redemption which is essentially equivalent to a dividend.

One of the principal problems with the proposed regulation is its length and complexity. It is over 40 pages in length and contains a dazzling array of confusing and difficult to comprehend rules, subrules, exceptions, qualifications, definitions, safe harbors, and rules of convenience. No one portion of the proposed regulation can be read without the necessity for reading and analyzing literally dozens of other definitions, exceptions, safe harbors, and so on.

Thus, the proposed regulation is extremely difficult to understand. Both professional venture capitalists and the operators of young, growing businesses will find it extremely difficult to comply with it.

Moreover, the rules contain a number of arbitrary, objective formulas, the application of which requires precise ascertainment of totally subjective and almost impossible to determine facts. Thus, as applied to specific business transactions, the proposed 385 regulation will prevent many transactions from being carried out and will raise substantial tax uncertainties with respect to others.

As a result thereof, on behalf of the National Advisory Council to the Senate Committee on Small Business, I would like to offer a resolution with respect to Regulation 385, as follows:

Whereas the Department of the Treasury delayed in issuing proposed regulations which would implement Section 385 of the Internal Revenue Code for 11 years;

Whereas the Department of the Treasury has now issued, over a two and one-half year period, three successive drafts of regulations to implement Section 385 of the Internal Revenue Code, each of which attempts to define the terms "debt" and "equity" for Federal income tax purposes;

Whereas the Department of the Treasury's latest draft regulations released on January 5, 1982, still create arbitrary and capricious situations that will (1) equitize the interest paid on debt instruments, thereby precluding such debt from being a deductible expense by the small business corporate payer, and (2) cause the repaid principal of the debt instrument to be treated as a dividend, thereby making such principal ordinary income for tax purposes;

Whereas the Department of the Treasury's January 5, 1982, proposed regulations are 40 pages in length and contain a dazzling array of confusing and difficult-to-comprehend rules, subrules, exceptions, qualifications, definitions, safe harbors, references to multiple other sections of the Internal Revenue Code, and rules convenient only to the Department of the Treasury and the Internal Revenue Service;

Whereas the proposed regulations will undeniably impede the capital formation process of young, growing businesses and mature financially-troubled independent businesses; and

Whereas the flow of capital to these businesses is essential to the renewed vitality of the American economy: Now therefore be it

Resolved, That there be an immediate introduction of legislation to repeal Section 385 of the Internal Revenue Code, to be followed shortly thereafter by joint Senate Small Business and Senate Finance Committee hearings to examine this critically important issue and consider favorably reporting the measure introduced.

Mr. MUDGE. Thank you very much, Mr. Hopewell. Would you like to make any additional comments?

Mr. HOPEWELL. With respect to section 385, of course, the information I have been able to glean from many accounting firms that are interested in the tax aspects is that it has been, on its face, a very confusing regulation. The IRS has not proceeded to implement this over an 11-year period. I think the alternative would be to go back to deciding various issues contained in section 385 on a case law basis, as in the past. That would be the comment I would have.

Mr. MUDGE. I am a director of SBANE, one of the 17 regional members of Small Business United, a small business grassroots volunteer effort. The organization is very much concerned about the regulation. It has had several meetings with Treasury representatives and has met recently with the Legal Counsel for the Vice President. SBANE is quite concerned with the impact this will have on venture capitalists, on spinoffs of multinationals, or in the normal processes of certain firms, particularly those who might be in the agricultural business. If one is a peppermint or spearmint producer in Illinois or Michigan, you generally borrow from June until October, and your debt equity might very well exceed four or five times. It could very well destroy businesses of that nature.

Senator NUNN. The only question I would have is, what would be the case law on that subject if you did repeal it? Are you saying the case law would be much more favorable?

Mr. HOPEWELL. What we are saying is that the specific issues that would be decided through the courts would not necessarily be more favorable, but it is very restrictive as 385 is written now.

Mr. MUDGE. Mr. Stout, have you had any anxieties about this?

Mr. STOUT. Yes, I certainly have. I have not been able to get very much information on the proposed 385 regulation, and most of the people that I have asked about it have not really understood what has been involved. The thing that bothers me is, if you are trying to expand and promote a business and borrow money, and if it is considered as going into equity, and if your interest payments on that cannot then be deducted as a cost, because that is also considered as going into equity, it seems very counterproductive to borrow money to try to improve and expand the business. That is about all that I have been concerned with or know of. I am glad to see we are spending some time on it.

Mr. WOMACK. It seems to me that one other aspect has not yet been considered. In fact, if the Internal Revenue Service is allowed to implement 385, it may open up a whole bag of worms. If the proposed 385 is allowed to become effective and if Treasury considers in fact borrowed money as equity, and the business then goes bankrupt, does the lender have a position and responsibility in the bankruptcy of the corporation? These are the kinds of issues that are coming forth and should be examined. The implications of this rule could be disastrous. It would put us in a posture, in the small business community, or in large businesses too, where no one would want to lend money simply because of the extended liabilities.

Mr. MUDGE. Would you like to move the resolution, Mr. Rhoads?

Mr. RHOADS. I would like to move that the National Advisory Council of the Senate Committee on Small Business adopt a resolution submitted by our friend from New York.

Mr. STOUT. I will second it.

Mr. WOMACK. Are we moving for repeal as you have described it?

Mr. HOPEWELL. Yes.

Mr. MUDGE. The resolution has been distributed. All those in favor, signify by saying aye.

[Chorus of ayes.]

Mr. MUDGE. Opposed?

[No response.]

Mr. MUDGE. The resolution is approved. Thank you very much, Mr. Rhoads and Mr. Hopewell for preparing that.

Mr. RHOADS. I have just a few more comments on the capital formation area.

This morning we heard that the budget negotiations are still going on. We do not have any idea where they are going to lead us, but we do know that part of that negotiation is going to result in some revenue enhancement recommendations being made to this body and the House of Representatives. From where I sit, the small business community has an overriding concern that if revenue enhancements are indeed passed, they will be at least sized neutral with respect to their impact on the business community. I suspect that at least the conventional wisdom now is that the budget negotiations will have some effect on the business tax provisions that were enacted under ERTA. If this happens, the small business community feels pretty strongly—at least this is what I hear in our area—that these revenue enhancements be at least sized neutral, that is that they should not disproportionately affect the independent entrepreneurial sector of the economy.

I say this in the context that the Tax Reform Act as passed was perceived by many of us as not being as sized neutral, as it might have been, and that perhaps some of the provisions that were passed to help business out, while necessary, might have been a little bit more weighted in favor of the larger capital-intensive businesses. I think we would hope that in the event proposed revenue enhancement comes from the business sector, small businesses do not get nailed again, or at least that small firms will be treated on an equal basis. That would be one comment that I would like to make.

Senator NUNN. As the Finance Committee gets into its deliberations, who can speak on the subject for the small business community? Do you have someone who can keep up with it in detail and alert us?

Mr. RHOADS. I believe we have a number of organizations who have folks watching that, Small Business United being one.

Mr. MUDGE. And SBANE.

Mr. RHOADS. I suspect that cuts across the spectrum of small business organizations, those three national groups or regional groups may be consulted, too. Those three would pretty well cover the waterfront.

One other point I wanted to make was, although the present budget situation renders it unlikely that there will be new legislation affecting Tax Code provisions, there is one concept being considered by the House and also by the Senate, which came out of the White House Conference on Small Business, and which many of us feel is a very good measure and needs careful consideration and early passage. It is the idea of a small business participating debenture, which affects a modification of the Tax Code and the securities laws to create a new instrument that will become kind of a label for allowing participation by investors in small businesses, without the entrepreneur having to give up an undue amount of control. The return to the investor is the up side, a piece of the up side potential, and in addition to that, a favorable tax treatment on that investment. That is, in a nutshell, what the small business participating debenture proposal would do.

There have been several versions of it introduced in the House and the Senate. I think, from my listening post at least, that it deserves some careful consideration.

Mr. MUDGE. Would someone else like to comment on Mr. Rhoad's two subjects? The SBPD was 1 of the 5 or 10 top recommendations of the White House Conference. It has been heavily researched and studied by the various organizations, including SBANE, IBAW, or SBU. Thank you very much, Mr. Rhoads.

Mr. RHOADS. Thank you very much for the opportunity.

Mr. MUDGE. If it is satisfactory, we will move on to the next subject. Senator Floss from the State of New York will discuss economic development issues.

REPORT ON ECONOMIC DEVELOPMENT

Mr. FLOSS. The two things I thought may be of interest are capital and industrial revenue bonds. Bob Dotchin, of course, gave quite a discourse this morning on what was being done in these areas. However, I will go into some of the things that I feel are important, be-

cause I have had some experience in industrial revenue bonding, having founded the first IDA in the State of New York, which today is very successful. I can also provide a lot of documentation about its success at any time.

One thing we did was to self-impose certain rules. One rule was that the program would provide industrial revenue bonding for a new business that would provide industrial jobs. We specifically incorporated a provision in our by-laws stating that we would never entertain a retailer, because a retailer only has so many dollars to go after within a community. I know that some of the criticism about IDB's centered around statements that they were used for hamburger stands or similar things, and that makes the whole thing look bad.

That may be throwing out the baby with the bath water. There is good, but there have to be certain constraints on the types of activity that you fund with IDB's.

In an attempt to minimize revenue loss, the Congress is considering here a proposal that small issue pooling be eliminated from industrial revenue bonding eligibility. I know there has been a lot of discussion and complaints by the small business community because of this proposal. As a result, in February of this year, the Treasury Department revised their proposals.

The new proposals are, as follows: To reduce the benefit from tax-exempt bonds by requiring a choice between tax-exempt financing and the accelerated cost recovery system; or limit the use of small issued bonds to small businesses; or arbitrage limitations would not apply to temporary construction period investment and reserve funds investment.

As you will notice, pooling is still limited. It seems to me that the first option does not exist for small businesses, because they are not making a profit for which to take any advantage on accelerated cost recovery. But startup businesses which are expected to create new jobs go through a long period without making a profit. If pooling is unavailable, then the cost of processing small bond issues outweighs the tax exemption benefits. I have found from practical experience that if a bond cannot be issued for over $750,000, the cost of going to bond markets exceeded the value. If we lose the effect of pooling, we then are removing that advantage for small business.

As I said before, it is my opinion that the problem of IRB's is not that small business uses them, rather it is the wrong kinds of business, large or small, that benefit from them. The purpose of these issues is to create new jobs. Consequently, the only businesses that should be able to benefit directly from an IRB are those that create jobs, not shift them. Manufacturing and processing are all job-creating activities; they bring jobs into a community employment for those people who are not already employed. In turn, these people put their money into the community. On the other hand, retailing and most service businesses bring nothing new to the community except competition for the existing pool of capital and existing merchants.

If the retailers are provided with lower costs from the use of IRB's, it becomes unfair competition. I agree totally with the President that unproductive draining of the Treasury must be stopped. However, I firmly believe that the tax revenues derived from people who have new

jobs will more than compensate for the lost income from tax exempt bonds. The solution is to issue the bonds for those who will generate new jobs, but not for those who will only transfer jobs from one place to another. If this is done, the result will be new jobs, a larger capital pool, new markets for new retailers and service industries, leading to more new employment and not more job shifts. The bottom line is higher tax revenues from all of these new workers and businesses, which will more than compensate for the revenue loss through the issue of IRB's.

Having recognized that small businesses in the aggregate are the most prolific producers of new jobs, we should permit small business, in the aggregate, to obtain the capital necessary to produce those jobs. By removing the tax exempt statuses of aggregate bonds, the IRS is in fact closing the door on most small business. If the Internal Revenue Service feels that IRB pooling should be stopped, then they should do it all the way down the line, because as it stands, it only benefits large business.

If the IRS feels it is good policy, is it fair? It is actually unfair for our tax policy to discriminate against small businesses. That is my view on that point.

We expect a great deal of economic development from the enterprise zone proposals. I have had no experience with enterprise zones yet, since we do not yet have them. However, coming from a State that has high unemployment, I am looking with great interest at the proposals, and I think I will offer certain thoughts for further discussion and investigation.

The concept, of course, is simple: offer substantial tax benefits in order to include business to move into an area of the country which is severely depressed. Zones are small, concentrated pockets of high unemployment. The expected success of this concept is predicated upon the idea that business will move to a low tax area primarily because of the tax advantages. Unfortunately, history does not support this assumption. Virtually every survey that has been conducted on the subject indicates that taxes are well down on the list of priorities when a company decides to relocate, expand, or startup. The first consideration, depending upon the type of business, involves market location, raw material, transportation, and perhaps the biggest consideration, labor.

Taxes enter into the equation only after these other needs are met. With this in mind, one should consider where the enterprise zone will be. All of the proposals that I have seen or read about define zone-qualified areas as parts of the country with very high unemployment and decaying or nonexisting infrastructure, whether it is highways, buildings, sewers, and so forth, and few, if any, raw materials. In most of these high unemployment areas, the skill level of the labor force is very low, be it rural or urban.

It seems to me that offering tax breaks alone will not be enough to attract business from another State or region of the country. State and local governments must be willing to commit educational facilities to train the labor force and improve facilities for transportation. I am not saying that this is bad, but it is expensive. Are those municipalities willing to look for the funds to do these things that are going to be necessary?

As many as you know, enterprise zones have been tried in England. One interesting fact is that the vast majority of companies that moved into these zones moved less than 1½ miles. Remembering what was said earlier, taxes only come into consideration after market and transportation and labor issues are resolved. It is logical that companies near these zones have already met these considerations and look upon the huge tax break as a true incentive to move.

If these zones are truly successful, we may look forward to an exodus of business and their taxes from the suburbs back into the cities in which most of these zones would be located. Congressmen and State legislators who represent nonenterprise-zone constituents may not find that this prospect is very appealing.

I now leave this session with a question. Does the enterprise zone concept represent economic development or economic redistribution?

Mr. MUDGE. Thank you very much, Mr. Floss.

Senator WEICKER. I suppose the aspect of the enterprise zone concept that is going to be the most troubling is the statement we hear, "Let's get the big companies out of it." Incidentally, I am not necessarily willing to accept your definition as to what brings jobs into a community and what does not. I am just not prepared to accept it as you have defined it. I am not so sure that retailing, food services, and other things do not create jobs: I think they do.

In any event, what do we do about those situations where the local business is under the umbrella of a larger entity? Let us take one that comes to mind, such as McDonald's. Why should a franchise business not be eligible? Should not someone who starts a McDonald's franchise be eligible, even though, admittedly, he comes under the umbrella of a far larger corporation, one that does not need IDB help? However the fact remains that the individual businessman may need such help.

Mr. FLOSS. That was not the point I was making about size. Looking at it another way, a retailer will always move where his market is. He can do that without any help.

But to bring in industry to start up, with capital needed for plant equipment, which will truly create new dollars in that community, which spins off to everybody I think is a desirable thing. But take a McDonald's that is going into that community where there are only so many dollars available. The franchise is now going to compete for them. Yet a Burger King may be in business a mile away. If McDonald's goes in with a tax advantage that he can spin off into lower costs, he then may be able to put the other fellow out of business. When Burger King's employees go over to work for McDonald's, you have created no new jobs, and you probably have less taxes all the way around.

Take a hotel, for example. A hotel will not go some place unless there is a market. Yet I know we have encouraged hotels to take advantage of this. I know they have done this in New York State. They go there because the market is there, and you do not need the inducement of the IRB to create new jobs. I do not think a retailer goes in just because he is getting a better break on financing; he goes there because the market is there. He will go there anyway.

I feel that with only a given number of dollars in an area to compete with, a Sears, Roebuck & Co. should not get a break and put K-Mart

out of business in that area and just transplant the employees. That is what I was referring to about the type of business.

Mr. MUDGE. Are there comments?

Mr. WOMACK. In regard to the IRB's, I would like to share with you some information of things going on in Texas that might be of some concern here. The State of Texas has chosen to differentiate between commercial ventures and industrial ventures. If in fact it is a commercial venture, then the entity, being the city in which the industrial revenue bonds are to be issued, must be declared blighted.

A blighted area such as the one in which I live, could have been flooded, and because of the flooding it is difficult to draw people into that particular area to set up facilities. The city of Houston has done the same thing. It has chosen particular areas within the city which are undernourished, if you will, decaying, or things of this nature and declared those areas blighted. They have been made available for commercial ventures as well as for industrial ventures.

Commercial ventures are only available in blighted areas; they are not available otherwise. An industrial area, however, can be put anywhere in the city where the zoning and so forth will allow.

Mr. MUDGE. Mr. Lefkiades, do you have any thoughts from Michigan? This might be a concern to business in your State.

Mr. LEFKIADES. Yes; I would like to comment first on the issue of McDonald's or the larger chains that were mentioned here. The real tragedy, of course, is that they are really not hurting Burger King, their largest competitor, or Kentucky Fried Chicken. The real tragedy is that they are getting all those tax benefits and inducements to locate where they are really hurting a mama's grill or a papa's grill and the other small businesses in the area that are really having a very tough time and finding it very difficult, particularly in today's circumstances, to compete. We have large, multibillion dollar corporations, with expert staffs, taking advantage of those programs and locating there, not creating new jobs per se, but taking business from the existing small businesses within a community and shifting the jobs within the community.

I would be inclined to agree with the gentleman from New York.

Mr. MUDGE. Thank you. I would like to call on Mr. McKenzie from Atlanta, who is close to this issue too.

Mr. MCKENZIE. Mr. Chairman, my 5-minute report substantially echoes Mr. Floss' report, but I have also been given the task of speaking on economic development from the standpoint of a minority businessman and a small businessman.

I have recognized several programs which have been in existence in the past, which have aided me in the development of my business. I have also tried to recognize those types of laws that, if enacted, could have assisted me but which failed to pass in Congress for one reason or another. I have great fears because traditional forms of economic assistance to the State and local community are being severely cut back because of the budget crisis that we are facing.

Programs that have traditionally helped business persons like myself get started, such as the Department of Labor manpower program, the Public Works business deevlopment program, HUD's urban development action grant program, and the Small Business Administration's programs are being drastically cut back by this administration.

All of these cutbacks, from my perspective, signal a radical departure by the Federal Government from decades of economic and social activism.

Essential to the administration's budget and tax cut initiatives is the conviction that the proper prescription for our ailing economy is massive reduction of spending, steep cuts in individual and corporate tax rates, coupled with regulatory reform. As a former pharmacist, I view the Government's prescription as a placebo, having little or no effect in a positive way. All of these cutbacks are going to make it extremely difficult for local and State governments to pick up the responsibility of providing such needed services as water and sewer, adequate transportation, and police and fire protection. All of these are essential ingredients for those plants or facilities that are thinking about locating or expanding their activities. Unfortunately, it appears that local municipalities are not going to have the revenues or the resources to replace the lost Federal dollars to provide these ingredients.

In construction activities, rehabilitation, and improvement of public facilities, including land acquisition or the kinds of key activities needed in any area for true economic development, if you do not have these kinds of components underway, you are not going to be able to attract the jobs that you need for an area. For example, the enterprise zone proposal that we discussed earlier, as presently conceived, offers some real incentives for businessmen in the form of tax credits and the reduction of the corporate income tax rate. It has received so much support because of its reasonable price tags. However, without the other services I have talked about, which are the public infrastructure needs, I am very skeptical that this concept is really going to have an impact on distressed urban and rural areas.

Furthermore, the absence of Federal economic assistance would probably assure that only well-established companies, with a solid financial backing, would be able to take advantage of newly created enterprise zones. Small businesses, the economic backbone of this country, would be effectively shut out of the potential opportunities inherent in enterprise zones. The fact remains that the Federal Government provides incentives to larger corporations, with Tax Code breaks, through publicly subsidized low-interest loans, and now through accelerated depreciation schedules.

Therefore, it is my position that in order to foster and encourage the economic development and growth of minority businesses and other small businesses, adequate provisions should be incorporated into enterprise zone legislation for Federal financial assistance. This approach would be entirely consistent with what the Federal Government has done for large corporations.

A concern with enterprise zone legislation as it now stands is that the tax incentives and legislation appear not to be strong enough to offset the cost of operating a business in a depressed area. Urban planners argue that market accessibility, not tax incentives, is the primary locational determinant for any kind of business, and that the tax climate is only one consideration among many. Tax benefits are attractive only when a firm is earning enough profit to face significant tax liability. Most new firms must struggle through several years before they reach that position. In addition, there is the question of

whether it makes any sense at all to give tax breaks to entrepreneurs when they cannot find money to get into business in the first place. So a large question is whether or not the tax incentive will be any kind of stimulus at all to new small firms.

Zones should, however, be attractive to large multibranched firms—as you just mentioned with the Burger Kings—thinking about opening another branch. The accelerated depreciation incentives would tend to help companies with large capital investments and the substantial tax liability with which to depreciate them. These firms would employ local residents and custodians, unskilled assemblers, lab assistants, and clerical workers. But because the legislation does not provide for training the unemployed in new skills, no new facilities may be developed. There is legitimate concern that local residents will gain little more than low-paying entry-level jobs.

It is imperative that any enterprise zone legislation contain strong job training provisions, with special emphasis on job training that enhances upward mobility.

Finally, we are now into the second year of this administration's term, and we are just in the midst of the hearing phases on the enterprise zone concept. It appears it is going to be anywhere from 12 to 18 months before we actually get these things on line and the local governments are trying to provide some services. With economists predicting that more businesses will fail this year than in any year since the Great Depression, and the report several months ago that 440 businesses failed that week, compared to 291 the same time last year, how many will be saved by the enterprise zone concept. So, in effect, we are not going to have anything from an enterprise zone standpoint to really make a difference to many small and minority businesses for some time.

In the near future, large businesses will benefit more from the new investment tax credit rules. However, over the long term, small businesses might benefit to some degree if they survive. But it will take the average small business years to understand all the legislation, and even then only with the help of sophisticated advisers before they come close to being able to take advantage of the incentives. In the final analysis, the true success of our economy is critically dependent upon the preservation of real opportunity for small businesses.

Mr. MUDGE. That is very interesting. The Financial Times, published in the United Kingdom today, had an analysis of what had happened in a similar program in Britain. They came to the same conclusion that you and Senator Floss have come to, your comment that it applies mostly to those firms within a 1½-mile radius. I was surprised. These were the first negative comments that I have heard, since initially it sounded like a worthwhile program to pursue. Perhaps when more people begin to study this, they might wish to look at the British experience to see what light that might shed on enterprise zone proposals.

Senator NUNN. I also find it very interesting. I have not thought my way through the whole enterprise zone concept at all. A lot of other people are really wide open for suggestions. I think your suggestions are very timely.

Mr. MUDGE. In our State of Connecticut, we were the first to adopt the idea. It is too early to tell whether it is successful or not.

I would like to proceed apace, if we may, because the meeting will conclude at 4 rather than 4:30. We will have to speed matters up.

Please, Mr. Stout, you may make your comment.

Mr. STOUT. All I want to say is, I am sorry Mr. Boschwitz is not here, because I believe he is involved in the enterprise zone issue. I would like to ask him what his interests are and discuss what has prompted him to get behind this. I agree with these people—I do not see how it will do small business any good. It must be more appealing to large business looking to segment part of their expansion into one of these areas to get cheap labor, tax breaks, and so on. A small businessman cannot pick up his business and move it; it would be too expensive, and small businesses generally do not have enough resources to make a viable operation in an area like that.

Mr. MUDGE. Thank you. These have been interesting observations, and they will be helpful.

Mr. RHOADS. I tried for 2 years to put together a redevelopment effort in downtown Atlanta, which came to failure last year about this time. That was under several very attractive programs which we tried to put together to attract capital. We succeeded in attracting outside capital, but we could not convince our lending community that the lending part of that program should be favorably acted upon by them.

That really brings us to the questions raised by Therman and Walter. If all you have is a tax incentive, and you do not have something in there that is going to encourage investment, either debt or equity investment, in that area given my own experience, I have a great deal of difficulty seeing how the concept is going to work.

Mr. MUDGE. I would like to move along. Would you like to give us your comments on innovation?

Dr. Obermayer is from Cambridge, Mass. He is very active in the SBANE Task Force, out of which emanated the basic elements of the innovation bill. He is as well-informed as any small business person in the country on the matter.

REPORT ON INNOVATION

Dr. OBERMAYER. I am not going to talk today about a new legislative proposal, because this is an area where the Senate and this committee have done more than their part. The Small Business Innovation Research Act is a very important piece of legislation. It has been referred to as a "litmus paper" bill in INC. magazine. The bill, S. 881, a bill herded by this committee through the Senate, has 86 cosponsors and passed the Senate by a 90 to 0 vote. The support of this committee is critical to its passage in the House.

Senator Weicker and the other members of this committee have done an outstanding job in moving the bill through the Senate. They have been the most articulate advocates, even during the past few months while the bill has been reviewed by the House.

The bill has problems in the House. First, it was reviewed by seven separate committees, and each of these committees had its own vested interest and its own constituencies, each tried to remove the portions which would affect its constituencies from the bill. It has been opposed by many universities and by the American Electronics Association, but

it has a lot of supporters in the House. In fact, there are over 200 cosponsors of the bill in the House. Currently, it is coming out of the separate committees and going to the Rules Committee, and we are hopeful that it will be on the floor of the House by the middle of May. I am sure there will be active discussions. The chances of the bill passing are very large, but the bill may be completely emasculated and not serve any purpose. It is not so much a question of will the bill pass, but will a meaningful bill pass?

This week there was an article in the Wall Street Journal about it. Other Articles have appeared throughout the media. We have seen much more public exposure on the legislation than any of us anticipated. Much of the exposure has been generated by the very intense opposition to the legislation by universities.

Why has there been so much opposition? I think there are two reasons, one of which is obvious and the other is a very fundamental issue that has been obscured by a lot of noise. The obvious reason that there has been opposition comes from the university's self-interest. They do not want to see 1 percent of the R. & D. budget of major agencies go to small business innovation research programs. As Senator Rudman said, in the best statement I have heard on the subject:

> The kind of greed and avarice he has seen from the basic research community is the kind he would have only expected from the oil companies.

That has been reprinted and quoted in many places and very well describes the situation.

The universities are afraid of losing 1 percent of the R. & D. pie. But the way they should be looking at it is an enlarged pie. In the long run, this legislation will lead to increased recognition of the value of basic research to our society. Small businesses provide the linkage between basic research and practical application. The role of the innovative entrepreneur is to convert laboratory curiosity into products or processes that will benefit mankind. That is the obvious answer to the obvious objection.

But the more fundamental objection to this legislation is in fact more disturbing, and should disturb every small business person. It relates to the power and control of big institutions. By big institutions I mean big universities, big hospitals, and big business. It is the power not only the power they seem to have over the direction of Congress but, even more importantly, over the people who work for the large institutions. This bill would, in fact, provide the seed capital to enable a person working in a large institution to start off on their own. That is very much a part of the concept.

If a person has a good idea, he can submit a proposal to the appropriate Government agency. If the idea is related to a national need, it can be competitively selected for funding. It does not matter what kind of institution the person is associated with. It really is related to the idea, the approach, and its value. It provides an opportunity for individuals to achieve the "great American dream" of starting their own company, of being an independent entrepreneur. We may applaud that, but large well-established institutions are afraid of that.

Most of the companies that have received National Science Foundation contracts under the program thus far have been not only small,

but very small. The average company has under 10 employees, and in many cases it has been one individual who submitted a proposal that was funded, and it provided the initial seed capital the firm needed to get going. This is certainly an anathema to large institutions. They may lose some of their institutional power to hold their best people within their fold. And it is the best people who get frustrated in large institutions and who want to start off on their own.

This act will indeed generate spinoffs. That is why the American Electronics Association is opposed to it, and that is why many of the universities are opposed to it. They have seen spinoffs in biotechnology, genetic engineering fields, where people leave universities, start their own companies, and do well. People within universities are concerned about this.

I think the message has not gotten through effectively to the small business or the public that this really is the key issue underlying opposition to S. 881. It is a fundamental one that should be brought out into the open. I do not think there is any point discussing the legislation further at this point, but I would be glad to answer questions. Most of you probably know quite a bit about it already.

Mr. MUDGE. Thank you very much, Dr. Obermayer.

Senator WEICKER. If Warren Rudman were here, I know he would like to thank you for your remarks. I could not agree with your remarks more. I do not know why, in God's name, both the Washington Post and the New York Times took after this thing, unless someone talked to them and they did not have a chance to hear your remarks. I wish they were here to listen to you.

Mr. WOMACK. Why don't we send a copy to them?

Senator WEICKER. I think that is a good idea. If I have ever seen people philosophically who are not looking for any set-asides or any special treatments, it is the men and women in this room. You truly are an independent group and, philosophically, very conservative on issues such as this. The thrust of the editorials that have appeared against it is this is some special grab-bag for small business. I have not seen small business yet ask for any special grab-bag. I think the broad principles, as were discussed here, are what motivated support of it. I think you are right: it is a good idea.

Mr. WOMACK. I would like to move that we do that.

Mr. MUDGE. Mr. Womack, we can just take the comments being recorded today, and transmit them with a covering letter.

Senator WEICKER. Yes.

Mr. MUDGE. All those in favor?

[Chorus of ayes.]

Mr. MUDGE. Opposed?

[No response.]

Mr. WOMACK. Could we research and find out who wrote the other articles, sir, so that we see that the right people get it?

Mr. MUDGE. Yes.

Mr. LEFKIADES. I would like to make a comment. Perhaps there is an explanation why the Washington Post and the New York Times took such a position. Traditionally, they have a large feedback from the academic community, and there is a strong connection between those

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newspapers and the academic community. Perhaps the articles were written by some of their friends in the academic community.

Mr. MUDGE. Thank you. May we move on now to Frank Ravel from California, who will discuss the matter of antitrust, which is of high concern to small business, particularly because of the activities of the last year.

REPORT ON ANTITRUST LAWS

Mr. RAVEL. I will speak to you on the importance of the antitrust laws in relation to our society and small business.

The antitrust laws were created mainly to protect our society against the abuses of the powerful trust monopolies and cartels. These laws are important because they are the safeguard of the general consumer, the large and small businesses, and the whole society in general. The antitrust laws are a blessing for all of us. They protect all of us involved in the U.S. free enterprise system, by giving us freedom to operate a large or small business. Without the antitrust laws, a large number of small businesses would become endangered species and eventually would disappear.

The Robinson-Patman Act became law in 1936. It deals with price discrimination and trade regulation. If a manufacturer decides to give a special price to one, he has to offer the same price to all. If a large customer comes in and says, "I will buy 100,000 Apple computers from you, the Apple Co., and I will make you an offer at 25 percent below what a regular dealer buys," this large conglomerate can retail these computers to the public, the end user, below the regular price to the small dealer. The small dealer would not have a chance to survive. These are the protections offered in the Robinson-Patman Act.

The Robinson-Patman Act, I understand, is poorly written. But regardless, it is on the books, and it is the law. It is illegal to use price discrimination.

The Sherman Act of 1890 is a strong antitrust law and deals with monopolies and the restraint of trade. Its most familiar passage is section 1, which reads: "Every contract, combination, and a form of trust or otherwise a conspiracy in the restraint of trade in commerce among the several States or with foreign nations is declared illegal and can be punishable by 3 years imprisonment and $100,000 fine."

I have always thought that when I purchased goods from a manufacturer or a supplier, these goods become mine. I can dispose or do whatever I wish with them. I paid for them. I can give them away or throw them in the ocean, if I wish, sell them to whom I wish, and sell them where I want, at any price I wish to sell them for, and ship them to any place I choose to ship them without interference from the manufacturer. This is what the Sherman Act, section 1, is all about. It is a marvelous tool for free enterprise, for the small business, and for business in general.

During various administrations, either Democratic or Republican, these laws have been in effect and highly respected by the Antitrust Division and they have been strongly enforced. About a year ago, the new administration decided to make some changes. They appointed a certain Mr. William Baxter, who previously was a law professor at

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Stanford University in California, to head up the Antitrust Division. It is a very powerful post.

Unfortunately for us in our society, for free enterprise and small business in particular, Mr. Baxter has worked and adopted a strange philosophy regarding the present antitrust law. His theory is to dismantle and eliminate all the present antitrust laws we now have and let the big boys swallow the little guys. Here are some of his concepts.

On March 4, 1982, I had the opportunity to meet with Mr. William Baxter in his office for 90 minutes. Mr. Baxter had the audacity to tell me, point blank, "The Robinson-Patman Act is an abomination and should be eliminated as soon as possible." Mr. Baxter is, of course, strictly in favor of big business. The Sherman Act also was not good for the country and should be dealt with. Mr. Baxter had the courage to tell me that a manufacturer or supplier can dictate to his dealers any terms, any conditions he wishes, and also can cancel the dealer at any time without notification. A manufacturer can dictate to his dealers about whom to sell, for how much to sell, where to sell the goods, when to open the store and close it, and that no law should interfere with the wishes of the supplier. The only right that the dealer has is not to buy the goods from the supplier.

Due to the present climate in Washington and the leadership of Mr. Baxter, the whole Antitrust Division is being destroyed. The result could be catastrophic for our society in general and, above all, for small business.

I mentioned to Mr. Baxter that there were antitrust laws on the books today. I asked Mr. Baxter, "Did anyone change these laws?" "Are these laws still active? Are they, the Robinson-Patman and the Sherman acts, still on the books?" Mr. Baxter answered, "Yes, they are active and they are on the books, but I refuse to enforce these laws, and I do not believe in them." What kind of talk is this, coming from a man who is in charge of the important post of policing and enforcing these laws. It is hard to believe.

Now I have a case going with the Apple Computer Co. That company has set a fund for $10 million to fight me, to make sure that they can get away with violating the actual and present antitrust laws. They have a large firm of 50 attorneys. Among these attorneys are young attorneys who were students of Mr. Baxter. They have been taking my depositions for the last 6 days.

Off the record I said, "Mr. Rabath, do you know Mr. Baxter?" He said, "Yes." I said, "Did you study under Mr. Baxter?" He said, "Yes, and many of the lawyers we have in the firm have." "In other words," I said, "Mr. Baxter has contaminated you with these theories?" He said, "Yes." This young lawyer is the most obnoxious and vicious lawyer I ever met in my life. Eventually we are going to beat them in civil court. We have enough evidence to do that.

Why should Mr. Baxter be permitted to call these lawyers in Washington, because he knows them, and then give them his blessings, saying if they do this or this, it is permissible to violate the law? This is beyond my comprehension.

After about 80 minutes of talking to Mr. Baxter, it seemed like I was talking to a cement wall. I was looking at a man who had no movement. He was listening to me. Finally, during the last 10 minutes, an idea

occurred to me. I said, "Mr. Baxter, what would happen if I could prove to you and bring you the evidence that the Apple Computer Co. is not policing and enforcing the new modification of agreement they made all their dealers sign, whereby each Apple dealer cannot accept a telephone call for an order?"

The agreement says that you cannot accept a telephone call. You cannot ship by UPS. You cannot ship by truck. You cannot even deliver the Apple product to your customer. He must have a face-to-face contact. He has to say, "Here I am." And he has to pick up the Apple product himself, otherwise he is violating the rules, and the dealer's contact can be canceled.

I spent about $30,000 opening up a service department to service Apple products. I have six stores. Only one of the stores, the main office, does mail order. The other five stores do not do mail order. I am a man of principle. I will not accept this condition. I received a letter contract can be canceled.

You are terminated for violating the modification of the dealer's agreement, and you are canceled for selling Apple products through main order.

But they canceled my contract at all six stores, not just one. That means the other five stores were guilty by association, and that happens to five other plaintiffs. They had four stores, and they canceled them all when only one store was responsible.

So I had to prove to Mr. Baxter that this contract was a subterfuge to eliminate discounters and mail order businesses who were saving lots of money for school districts, universities, colleges, and consumers. I created a school on paper, called the Montessori School for Gifted Children. I mailed 1,100 requests for quotations to all Apple dealers. Believe it or not, we received 300 answers saying, "We will sell." I have them. I brought them to you, and I gave them today to Mr. Brian Hartman.

All these dealers said yes. They bid $7,000 or $8,000 for all the products, and I sent another order for software, to make sure that if one was scared to bid on the hardware he would bid on the software.

Mr. MUDGE. Excuse me, sir. Could you wrap this up in 1 minute?

Mr. RAVEL. Yes; finally, we got the answer. I sent everything to Mr. Baxter. I expect him to do something. Meanwhile, Senator Strom Thurmond and Representative Rodino, who chair the Judiciary Committees in both Houses, are very much interested in the case.

Mr. MUDGE. Thank you very much, sir.

Would anybody like to add to that, or shall we move to the next subject. I do not mean to cut it off, but I am keeping my eye on the time.

Senator NUNN. Your story has a lot of credibility. We did have Mr. Baxter before our committee, and we also heard from him.

Mr. MUDGE. Mr. Womack, would you be good enough to give us your views on the economic outlook?

REPORT ON THE ECONOMIC OUTLOOK

Mr. WOMACK. I chose not to write anything up today, because after I looked at what we were going to be doing, I felt I needed to listen to what other people were saying in the room. The things I needed to say need to be somewhat related to the things mentioned here in other areas.

The economic outlook obviously encompasses capital formation and retention, taxes, economic development, innovation, export, antitrust, and all of the other things we have touched on today. Along with this, though, there seems to be an overriding theme that affects all of us. I think maybe we ought to take a moment or two to quickly examine the real costs of the high interest rates, what they are doing to our economy, to each particular individual, to the tax structure of our country, and our ability to exist as a nation; what is the real cause of high interest rates; what kind of a negative effect have they had and what kind of a positive effect have they had. Believe it or not, there are, in my opinion, some positive effects.

Reviewing quickly the things I heard today, the primary culprit responsible for high interest rates is the Federal deficit. I have to go along with that, by and large. I think that the Federal deficit, has placed a real burden on the rest of the economy, in terms of consumer borrowing, business borrowing, the effect that OPEC has had on us for the last few years, and the quadrupling of prices. It is very difficult to quickly absorb into the internal structure of business. It has taken a while for us to digest it. Along with this, we were not able at first to pass on the cost, if you would, to consumers. This places a strain on the ability of a business to operate. Along with this, obviously, it places a demand for additional capital, which usually has to be borrowed if small firms are concerned.

Probably the biggest problem caused by high interest rates is a loss of confidence in Government, in Government programs of the past, and doubts as to what the future may hold.

With that sort of preface, I would like to comment quickly on the negative effects. With the high interest rates, we have a great loss in consumer demand. People do not want to borrow money to buy houses or cars or anything else because the rate is far too high. We have had a loss of jobs. Why we have had the loss of jobs is really very simple. As consumer demands go down, people cut back because they cannot afford to keep everybody they have on hand, the marketplace slows down, and people lose their jobs.

Then there is a loss of tax revenues. It is inevitable, on the Federal and the State level. As this occurs and there are cutbacks, people are out of work, there is a strain placed on unemployment systems. It is a ripple effect. It is dramatic.

One of the greatest tragedies of all is the loss of future technology, with the closing of businesses and with the laying off of people who are involved in particular research programs and things of this nature within small companies.

To that end, I would like to talk now about what high interest rates have accomplished with regard to the positive aspects. Someone told me yesterday that there were no positive aspects, that there was nothing worse in the whole world than high interest rates. I suppose that is probably true, but there are some positive things that have come out of it. One of them is the fact that it is beginning to educate our people that we cannot overextend ourselves any more, on a governmental level or on a personal level. Consequently, it is creating a new awareness, if you would.

It is going to bring a lot of innovation back to business, a lot of innovation that has been lost in the past by the fact that a lot of money is flowing through the systems all the time, readily available, with not as much attention paid to profits as perhaps there should have been. We have become somewhat more lean. We have begun to look at things a little differently and looked perhaps at better ways to do things than we have done in the past.

It brings back attitudes of quality, because we find that in some of the things that have been going on, when money is readily available, we produce and produce and produce, and if it is not bought really quickly, or if it is bought and it is used up quickly, then we would reproduce again. It is the great American built-in obsolescence.

Probably the biggest single advantage—and I am sure there will be some disagreement with this, but I see some very positive things from this, too—is that we are in the process of cleansing the system. We have to acknowledge the fact that there have been many companies that have been artificially propped up with governmental assistance, the ready availability of capital, and the fact that if someone is lost the system goes on. It seems to me that we are going to have a change in attitude, and we are going to have people who really have the opportunity to move forward, after we eliminate some of the companies that do not really belong in business anyway. And there are those types of businesses. It is hard for us to admit, because we are an enterprising Nation, but the fact is that it is true.

In summary, I would have to say that among the things I have heard here today, there is a general optimism. I share in this myself. There is obviously some pessimism, and some of that I share also. But the outlook, in my opinion, is really very good. I think we are going to see a very slow upturn. I have never believed that we were going to see a rapid upturn like we have had in the past, and I am not sure that that is really good for the country. The thing that I have noticed in my own concern, and I obviously relate to this more readily than anything else, as the upturn has come—and there is no question that it is increasing more slowly—it is a great deal more solid than it has been in the past. By that I mean, in the past I have seen very large sums of money pumped into the economy quickly, consumer buying picks up very rapidly, demand gets great for a while, and it looks like a camel's back with a bunch of humps in it. That is not what is occurring in my industry at the moment; it is a very gradual rise, and the things that are being bought are the things that are necessary. They are quality items. The increases are very favorable and very strong.

The lessening of credit demands is going to be obviously seen within the next couple of years, if what is going on now continues. As we gradually build back up to a posture where companies start to put people back to work, we will find that our tax basis is going to increase, and the Federal deficits and the State deficits are going to go down.

By and large, we are on the threshold of a new era. I think that we, as small business people, must have the intestinal fortitude to hang in there, to do the things that we have to do to make the climate better. To that end, I think that this committee is certainly making an attempt to achieve that. Thank you.

Mr. MUDGE. Thank you very much. Mr. Womack has been one of the keepers of the flame. He has been the centerpiece of the small business movement in Texas. His personal expenditure is peerless. I doubt if anybody in the small business movement has expended as much of his own money to promote small business as Morris has. We appreciate very much your coming up from Texas and making your observations. He has been contributing down there as well. There has been two State conferences that Morris has helped organize, carrying the small business message in Texas.

Mr. Lefkiades, would you like to make some comments?

Mr. LEFKIADES. First I would like to comment on Mr. Ravel's experiences with the Antitrust Division and Mr. Baxter, before I go to the subject that I am supposed to speak on. This present administration was elected, I believe, with the support of a large sector of the small business community. Unfortunately, Halloween is over and the mask is off. We are now learning about its true colors; that this administration is not helpful to the small business community. Its actions are detrimental to the interests of the small business community.

A very significant example of that is the appointment of Mr. Baxter to head the Antitrust Division of the Justice Department. We must recognize that there is an inherent conflict between big and small business, and a wolf has been installed inside the small business chicken coop. The Antitrust Division is not going to safeguard the interests of the small business community, unfortunately. It is fairly evident to everybody here. As Senator Weicker so eloquently stated, we thought we elected the party of Jefferson, Lincoln, and Eisenhower. Unfortunately, we now have in power the party of Jesse Helms. Their actions have been extremely detrimental to the small business community, so far as the Antitrust Division is concerned.

Now the subject matter which I was going to discuss pertains to the Federal Reserve and the process of selecting members to the Federal Reserve Board. Congress has not been vigilant in adhering to the provisions—if you will, the letter and the intent—of the 1913 Federal Reserve Act, which envisioned and provided that the members represent the full spectrum of the American financial, business, and geographical interests. Unfortunately, all seven present members are either former employees of the Federal Reserve—five of them—or have been affiliated with two megabanks. I question the wisdom of having such a group at the helm of the Federal Reserve.

There is a ray of sunshine in Senate bill 881, and I believe amendment 763, which provides that the next nominee to the Federal Reserve Board be a person with a small business background. I would like to see this body adopt a resolution and advise the Senate Small Business Committee to expand on that, to see that a balance of representation exists on the Federal Reserve by which the two inherently conflicting factions of the lenders and the users have equal representation on the board.

I believe that was the intent of the act when it was enacted, and I believe you should move in that direction.

Mr. MUDGE. Mr. Lefkiades, you have a good thought there with many interesting elements. I do not think that in fairness we can act precipitously on it, even though initially we may be very favorable

to it. May we just recommend that the Senate Committee on Small Business consider your thought, so we may move on. Would that be sufficient, sir?

Mr. LEFKIADES. Yes. Perfectly.

Mr. MUDGE. If no one minds, I would like to call on Therman McKenzie for one final comment.

Mr. MCKENZIE. I would just like to make mention of this. We are in the business of producting health and beauty aids for an ethnic community which comprises 12 percent of the population of these United States. But we are finding that the greatest population market for us is in the international area. Many times that is in the Third World countries. But the Third World countries put limitations on exports. They want you to basically make an investment right away or do a joint venture right away in those countries.

I was wondering if there is anything that could be done to help a small business which has a potential, and a product that can be widely used by millions of people in the continent of Africa and other places, by having a time span of maybe 5 years to export there, with the intention of investing some of the locally generated revenues through joint ventures later on. If we have that type of assistance, I think we can really help have an effect on the trade deficit of the country.

Mr. MUDGE. Thank you very much for putting that in the record.

Senator WEICKER. Not only in the record, but I wish my staff would follow up on that. I would like to hear more about it, because I agree with you.

Mr. MUDGE. I would like to thank Senators Weicker, Nunn, Hayakawa, Huddleston, Dixon, and Levin for attending and listening to our comments and observations.

I thank you all for taking the time and the trouble to come here. It is an example of small business at its best, at its grassroots. I know we speak from experience, and we hope that our comments will be helpful to those who deliberate and act in our interests.

The meeting is adjourned.

[Whereupon, the meeting of the National Advisory Council adjourned, to reconvene at the call of the Chair.]

[Additional information follows:]

AGENDA

NATIONAL ADVISORY COUNCIL MEETING
THURSDAY, APRIL 22, 1982

8:30 a.m. - 4:30 p.m.

8:30 a.m. - 9:30 a.m. 424 Russell Senate Office Building	INTRODUCTORY SESSION/TRANSACTION OF COUNCIL BUSINESS Coffee and danish available
9:30 a.m. - 10:30 a.m. 424 Russell Senate Office Building	ECONOMIC AND BUDGETARY OUTLOOK FOR 1982 Mr. Edwin L. Dale Assistant Director for Public Affairs Office of Management and Budget
11:00 a.m. - 12:00 p.m. 424 Russell Senate Office Building	GOVERNMENT REGULATIONS AND SMALL BUSINESS/ VICE PRESIDENTIAL REGULATORY TASK FORCE Mr. Boyden Gray Legal Counsel Office of the Vice President
12:15 p.m. - 1:30 p.m. Vandenberg Room U.S. Capitol	LUNCHEON Mr. James Sanders Administrator-Designate Small Business Adminstration
2:00 p.m. - 4:00 p.m. 424 Russell Senate Office Building	SENATE SMALL BUSINESS COMMITTEE MEETING Members of the Committee to meet and discuss issues with the Advisory Council

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